UNITED STATES-CANADA TRADE UNDER FTA AND NAFTA

Y 4. SM 1: 103-86

United States-Canada Trade Under FT...

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRD CONGRESS

SECOND SESSION

WASHINGTON, DC, JUNE 9, 1994

Printed for the use of the Committee on Small Business

Serial No. 103–86

APR 11 1995

U.S. GOVERNMENT PRINTING OFFICE

80–292 CC WASHINGTON : 1995

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402
ISBN 0-16-046831-0

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UNITED STATES-CANADA TRADE UNDER FTA AND NAFTA

THURSDAY, JUNE 9, 1994

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The committee met, pursuant to notice, at 9:35 a.m., in room 2359–A, Rayburn House Office Building, Hon. John J. LaFalce (chairman of the committee) presiding.

Chairman LAFALCE. The Small Business Committee will come to order. Our committee convenes this morning to examine the status of United States-Canada trade relations and how the two countries have fared under the provisions of the Free Trade Agreement operative since January 1989 and now subsumed into the North American Free Trade Agreement.

I was a strong proponent of the FTA in 1986, 1987, and 1988, and continue to believe it was an enormous step forward in liberalizing trade relations and promoting economic growth in both Canada and the United States.

Canada is the United States' largest trading partner, according to the U.S. Department of Commerce and to Statistics/Canada. Two-way trade has grown at double digit rates since FTA implementation, rising 14 percent in 1993 over the previous year to nearly $220 billion.

U.S. manufacturers increased their penetration of the Canadian market to 29.6 percent in 1991–1992, up from 26.4 percent in 1989 to 1990. Canadians also increased their manufacturing share of the U.S. market by one-tenth of 1 percent.

The trade agreement has further expanded trade opportunities between our two countries in services and government procurement through greater liberalization measures. New provisions also strengthen intellectual property protection and greater coverage of land transportation services broaden opportunities in this sector.

But even with the substantial increase in trade between our two countries, the lowering of barriers to goods, services and people flowing across our borders, and the impressive new cooperative efforts of like-minded groups in both countries, this important effort to enhance bilateral trade relations has not been without some problems.

The list of bilateral trade disputes is lengthy, and the dispute settlement mechanism has proved, according to some, somewhat cumbersome. As part of today's hearing, we want to examine whether the dispute resolution process that was negotiated and the United States Congress approved is operating as intended.

Questions have also been raised as to how the panels have functioned and whether they have followed the mandate of reviewing whether respective laws have been applied correctly, as opposed to whether the laws themselves are correct.

The committee is interested in ways the panel system might be improved to make the process for traders on both sides of the border an easier, faster means for resolving disputes.

Two weeks ago, Canadian Trade Minister MacLaren and USTR Kantor discussed the possible development of alternative trade remedy proceedings. We would like to hear from our witnesses what alternatives to trade remedy rules might be under consideration.

Obviously, changes to these procedures and the recourse in resolving trade conflicts they provide will affect the business community and small business in particular.

This morning to provide us with expert perspectives on United States-Canada trade, we have Mr. Charles Roh, the Assistant U.S. Trade Representative for North American Affairs, and as such, the key U.S. official directly responsible for our bilateral trade relationship. Mr. Roh was also directly involved in passage of the FTA implementing legislation in 1988.

We also have Mr. Paul Joffe, the Principal Deputy Assistant Secretary for Import Administration at the U.S. Department of Commerce, is responsible for overseeing U.S. trade laws and has close experience with dispute resolution panels.

Finally, we get a Canadian perspective, at least one Canadian perspective, from Professor Murray Smith, director of the Center for Trade Policy and Law at Carleton University in Ottawa, and he has very extensive experience in Unites States/Canada trade relations. We welcome all of you this morning.

Mrs. Meyers, do you have any statement to make?

[Chairman LaFalce's statement may be found in the appendix.]

Mrs. MEYERS. I would like to make a brief statement, Mr. Chairman. Today the committee conducts another session on a most important topic, United States-Canada trade relations. The world market is now truly a reality. This situation will undoubtedly cause some dislocation in all industrialized countries. To be competitive, nations must seek a pro-entrepreneurial outlook and reject antigrowth taxation, regulatory, and general government mandate policies. As our own country ventures forth in the new world atmosphere, we must do our utmost to secure fair and prosperous trade policies with our nearest neighbors first.

The United States-Canada Free Trade Agreement and the recent NAFTA agreement are two very positive steps in this direction. This morning we are focusing on our relationships with Canada. In reviewing today's testimony, I was particularly impressed with the statement of Murray G. Smith. Utilizing solid economic facts, Mr. Smith paints a very positive picture that has developed for both nations as a result of our trade agreement. He then goes on to make a most salient point. Many Canadian economists view the agreement favorably, yet the Canadian public itself has a different perception. In fact, many Canadians blame their country's lingering recession on the trade agreement. This presents policymakers such as ourselves a valuable lesson. It is a difficult task, at best, to

produce positive economic policy. Part of this task should include the education of the public with the appropriate economic results of each and every policy.

Thank you, Mr. Chairman.

[Mr. Meyers' statement may be found in the appendix.]

Chairman LAFALCE. Thank you. Are there any other members of the committee who have any statement they wish to make?

[Mr. Ramstad's statement may be found in the appendix.]

[Mr. Sarpalius' statement may be found in the appendix.]

Chairman LAFALCE. Then we will hear from the panelists. Gentlemen, we will put the entirety of your testimony in the record and you may feel free to either read it or summarize it, but hopefully either within 10 minutes or so. Mr. Roh.

TESTIMONY OF CHARLES E. ROH, JR., ASSISTANT UNITED STATES TRADE REPRESENTATIVE FOR NORTH AMERICAN AFFAIRS

Mr. ROH. Thank you very much, Mr. Chairman. I am very pleased to be here to testify on this very important topic of the United States-Canada trading relationship and the operation of our Free Trade Agreement with Canada, first under the United States-Canada Free Trade Agreement and then under NAFTA.

I will take up your kind offer to submit my full testimony for the record and to summarize. I would also like to express my appreciation to you because you have already covered some of the ground that I was going to cover myself.

I think it is worth starting out in any discussion of the United States-Canada relationship with the sheer enormity and success of the relationship before we get on to what unfortunately so often transfixes the media on both sides of the border, which are the little disputes, or the not so little disputes.

To the numbers you were expressing about the relationship, I would add a couple of interesting ones. Our exports of goods alone to Canada in 1993 passed $100 billion, and that is estimated to support some 1.65 million U.S. jobs. This is a terrifically important relationship to the United States.

It dwarfs our second largest trading relationship, which is Japan, and which is where the United States-Canadian relationship is well over $200 billion, that with Japan is about $150 billion, and of course that with Japan is far less balanced.

The success of the United States-Canada Free Trade Agreement, of which you were a major proponent, in many sense has led to the NAFTA, and let me just make a couple—note a couple of points on the NAFTA. Almost everyone focuses on the most important single thing in the NAFTA, which was the addition of Mexico to the free trade area, but the NAFTA also made a number of improvements, in our view, over the United States-Canada Free Trade Agreement in terms of the United States Canadian relationship.

We were able to negotiate stronger and clearer rules of origin, for example, which is a terrifically important point for small business and everyone else. There is a clearer and more predictable set of rules. In the course of those negotiations, we resolved some serious problems we had had with Canada about the auto rule of origin, for example, and we have not only increased the amount of content

that must come from North America from 50 percent to 62.5 percent, but the rule is clearer and more predictable and I think will help us avoid the kind of disputes that plagued us in the early 1990's.

Other things we have done have added world class intellectual property rules to the United States-Canada Free Trade Agreement. That was a missing element from the United States-Canada agreement. It is now in the NAFTA. We have clearer investment and services rules.

The environmental provisions of the NAFTA are a substantial improvement. We have made it absolutely explicit, the right of each country to protect its own environment, its own health and safety, and I think the NAFTA indeed got some support from environmental groups, which is rare in the days of free trade agreements.

We also were able to do side agreements on labor and the environment just this past year, which, for the very first time ever, we have North American agreements to improve environmental cooperation and environmental protection and in the protection of labor rights.

Much of the NAFTA, however, is for the United States-Canadian relationship, really an incorporation with relatively few changes of the provisions of the United States-Canada Free Trade Agreement. So, for example, our tariff schedule has remained the same and all the duties will be eliminated by 1998 between the United States and Canada.

The particular provisions we had on agriculture, on culture, on alcoholic beverages and wine, were carried forward substantially intact, and the dispute settlement mechanisms of the United States-Canada Free Trade Agreement were largely carried over to the NAFTA with some improvements.

I think my colleague, Mr. Joffe, is going to talk about some of the improvements to the provisions of Chapter 19, but one that I perhaps should note is that the investment provisions of NAFTA now provide for investor State dispute settlement, that is, they allow arbitration of disputes between a private investor, big or small, and the host government in international arbitration proceedings, as in the case of a court proceeding, it is something to be avoided if you can—we would all rather not have disputes, but it is an extra element that enables us to—parties of one of the NAFTA countries to obtain relief directly without having to go through their government if they wish.

Let me note that on management of the NAFTA, we have also tried to learn something from the United States-Canada process, and we set up right at the start in the agreement itself and in the first months of this agreement almost 30 working groups that are dealing with everything from worn clothing to a customs working group to a rules of origin group, several agricultural groups.

All of these groups, which are trilateral and trinational in character are intended to get the experts of each country together on a regular basis, and the purpose, the main purpose, is to avoid problems, to make sure that the implementation is on track, and that the experts are eyeballing each other every few months so you can avoid the buildup of problems.

The other function they have is where they find them, to make recommendations as to how can we do this better. You were speaking about dispute settlement resolution at the outset, Mr. Chairman. At the behest of Canada, we created two new groups on subsidies and dumping looking at the question of, is there a better way than we are now pursuing to manage those problems of subsidies and dumping and measures taken against them. That is a daunting task.

We tried that for a while under the United States-Canada Free Trade Agreement. I think it is a worthwhile exercise, but I don't want to promise instant results. We have a commitment to get a report from this group 2 years after entry into force of the agreement.

Chairman LAFALCE. After the FTA was passed in 1988, we had a 7-year timeframe to negotiate an agreement between the United States and Canada on subsidies, and I now do not expect instant results, seeing the process that is taking place, or nonprocess from 1988 through 1994.

Mr. ROH. The point is well taken. In fact, if I can digress just a moment, in fact, what happens, we had these groups in 1988, but we also had the Uruguay Round negotiations were ongoing at the time and both the United States and Canada came to agree that since we were negotiating on substantially the same topics in the Uruguay Round, we would focus our efforts on that multilateral effort.

I think the Uruguay Round did produce some new rules on subsidies, particularly less so on—perhaps on dumping, but the object of this new trinational group is to say, well, all right, now, let's look at those things and see if there is any better way we can manage this relationship.

How have we been managing the disputes? I think Paul Joffe is going to focus on Chapter 19, as I said. It is worth making perhaps at least one point about the Chapter 19 mechanism, which is this unique process by which we have agreed to have binational panels of private sector experts substitute for our courts in reviewing, under national laws, and under national standards of judicial review, final determinations of the administrative officers.

That is unique, and sometimes people say, well, you have so many disputes, the United States-Canada relationship is obviously worse because now you have had 50 cases and you got many more disputes with them than you have with any other country, but we don't have this kind of a mechanism with any other country, and those disputes that fall under Chapter 19 are not really intergovernmental disputes. They are a manifestation of private citizens on both sides of the issue in countervailing duty and dumping cases, in effect, exercising their right to go to court to appeal an administrative decision.

We have very few disputes, considering the size of the relationship, that are between the United States and Canada about the terms of the—of our free trade arrangement. In fact, only five cases have gone to a United States-Canada panel where the dispute is about the terms of our trade agreement.

The other cases are all in effect—it would be a fairer basis of comparison to say how many times have we had to go to court for

a—for review of a dumping or a countervailing duty order with Japan, because that is what the Chapter 19 process substitutes for.

So, I think it is worth noting that, that we don't have a more disputatious relationship, I don't believe, but rather we have agreed to have binational panels instead of courts look at this very important section of trade remedy law.

The other point worth noting is that the disputes that you don't settle, or while they are unsettled, get all the press attention, but we have had a number of substantial successes I believe in resolving matters on a negotiated basis with Canada.

A few years back, we had a dispute, for example, about salmon—the salmon and herring fisheries on the West Coast, and while that was a dispute, we managed to be big news in the newspapers and there was a long haggle and finally we came down with a 3-year deal about 3½ years ago, and this was the subject of newspaper editorials and so forth, mostly in Canada.

This year we quietly extended the agreement for a year on improved terms, and I don't think we rated page 12 of the business section of a single newspaper, which is only to say that the disputes aren't very interesting if you just manage them well.

But there have been a number of other successes.

Chairman LAFALCE. We still have some hotly contested fishing issues in controversy.

Mr. ROH. Oh, sure.

Chairman LAFALCE. Both the East and the West Coast.

Mr. ROH. I would freely acknowledge there is a salmon dispute that is not a trade dispute that is going on on the Pacific Coast right now.

Happily, that is not our bailiwick, you will have to get people from another part of the Department of Commerce here and the State Department to talk about that one.

Chairman LAFALCE. Try to figure out the United States' position, the Canadians' position and then the Alaska position.

Mr. ROH. Let the record show that I said nothing.

Let me wrap up by noting a few of these things. We resolved a 15-year problem on plywood standards. I wouldn't promise that it is definitive, but we have certainly made progress on the beer dispute, which in the old catechism of the United States-Canada relationship, it is known as suds and spuds, hogs and logs.

In the telecommunications area, a longstanding thorn in our side was the preferential supplier relationship between Bell Canada and Northern Telcom. That has been eliminated this year. We had a dispute on lobsters, which is now at least in a manageable form.

So, anyway, just to note that we have been working to resolve those disputes.

There are outstanding ones. They tend to be in the agricultural areas and the resource areas. I think the explanation for this is perhaps twofold. Governments intervene more in those sectors. They intervene on both sides of the border, so when you eliminate the border measures, it exposes even more clearly the differences in governmental policies in things like agriculture.

The other thing is that those tend to be the areas that we exempted from the Free Trade Agreement, or that we didn't address under the Free Trade Agreement in the free trade negotiations. So,

they are not that the FTA hasn't been working in a sense where we should be faulted for falling short of resolving those problems in the negotiations themselves, and the reason that we continue to dispute them, because it is so hard when they are important sectors for both sides, and it is very, very difficult for us to arrive at a solution, but we continue to work at it.

Let me just go back. I mean, it is almost a cliche of those testifying about United States-Canadian relations, but it remains true, that about 99 percent of the relationship is conducted very happily, that the disputes occupy relatively a tiny proportion of our relationship, and that doesn't mean we shouldn't continue to work on resolution. That doesn't mean we shouldn't continue to plug away.

It has produced some success and I expect it to in the future.

So, thank you.

Chairman LAFALCE. Thank you very much.

[Mr. Roh's statement may be found in the appendix.]

Chairman LAFALCE. I agree with you, it is important to underscore the point that 99 or 99.9 percent of the time we have the most excellent relations that are possible, and it is inevitable that there will be some irritants.

Of course the reasons I am having this hearing too is you always read so much about trade between the United States and every other country in the world. The trade between the United States and Canada dwarfs the trade with any other country in the world, any other country. We need to pay more attention to it.

Chairman LAFALCE. Our next witness is Deputy Assistant Secretary of Commerce for Import Administration, Mr. Paul Joffe.

Mr. Joffe.

TESTIMONY OF PAUL L. JOFFE, PRINCIPAL DEPUTY ASSISTANT SECRETARY FOR IMPORT ADMINISTRATION, U.S. DEPARTMENT OF COMMERCE, ACCOMPANIED BY STEPHEN J. POWELL, CHIEF COUNSEL FOR IMPORT ADMINISTRATION

Mr. JOFFE. Thank you, Mr. Chairman. I greatly appreciate the opportunity to visit with you and the committee today. I was not too many years ago a member of the staff of one of the committees of the House, and it is indeed an honor for me to return in this capacity.

Chairman LAFALCE. Which one was that?

Mr. JOFFE. The Commerce Subcommittee of the Energy and Commerce Committee. I am accompanied today by Mr. Stephen Powell, chief counsel, Import Administration, and Jonathan Doh, the director of Trade Policy for the Office of Canada and Mexico.

The trading relationship between the United States and Canada is of great importance to our economy. Of the many statistics one could cite, since the CFTA became effective in 1989, U.S. exports have shot up in sectors which previously faced high tariffs and in 46 of 98 product categories, exports grew 100 percent or more, and I would underscore that while trade frictions have not been entirely eliminated, they have actually been reduced in certain respects.

The number of antidumping duty orders issued has dropped from 12 during the period 1984 to 1988 before the CFTA became effective, to 8 from the period from 1989 to 1993. With this overall

sense of the relationship in mind, I would like to address certain developments under the CFTA and the subsequent NAFTA.

Three issues that I will discuss are the binational review process, the process in several specific cases, logs and hogs, as my colleague put it, and the prospects for the panel review process in the future under NAFTA. Let me say before I go forward, taking note of Professor Smith's presence here, and we look forward to his testimony, that in the dialogue that we are having relating to the Uruguay Round legislation which will shortly be submitted to this body, that in addition to all the many domestic interests that we have been speaking with, we have been conversing with the Canadian government and exchanging views and information about the operation of their system, as well as our system, and their views with respect to the coming legislation.

As the committee knows, we have under the CFTA and NAFTA the binational dispute resolution procedures, and a salient point of those procedures is that the binational panel reviews the law—the domestic law of the country in question and interprets that law, in contrast to the GATT panel proceedings that you are familiar with where our law is set against a standard of the international agreement.

Here the responsibility of the panel is to look at the case in the light of the domestic law. There is a review process, the so-called Extraordinary Challenge Committee, which is designed to protect the integrity of the panel process so that if certain criteria are not met, there will be a check on the panels.

As my colleague, Mr. Roh, mentioned, we have tried to learn from experience, and when NAFTA succeeded the CFTA, some improvements were made. An example of that would be that NAFTA includes a new process for safeguarding the panel review system. Specifically, article 1905 permits review by three-member special committees of allegations by one country that another country has interfered with the proper functioning of the panel system, for example, by preventing establishment of a panel or not enforcing a panel decision.

The panel process has been viewed by many exporters of both countries, both Canada and the United States, as very favorable. They have favored the process and while the Free Trade Agreement continues to allow a party to bring a case under the national court systems, it is noteworthy that the majority of parties have chosen to pursue the panel process.

Turning from that process to a few specific cases, I will briefly discuss the swine, pork, and lumber cases.

The Chapter 19 binational panel review process went into effect in January 1989, speaking on page 5 of the prepared testimony. Since that time, there have been 19 panel decisions issued in the United States and Canada in cases involving antidumping and countervailing duty determinations, for which my office has responsibility.

Of these 19 decisions, three have been challenged by the United States before the Extraordinary Challenge Committee that I referred to earlier. These three involve United States countervailing investigations of pork, swine, and lumber products.

The pork case involved a challenge to the International Trade Commission's threat of injury determination, while the swine and lumber cases involved primarily the issue known to the aficionados of this business as specificity. That is, they involved whether a subsidy has been provided to a specific enterprise, industry or group of enterprises or industries, which is a precondition under U.S. law, to finding a subsidy countervailable.

The ECC's, the Extraordinary Challenge Committees, in both the pork and swine proceedings dismissed the challenges—our challenges, the United States' challenge to these binational panel decisions for failure to meet the Extraordinary Challenge Committee's criteria for bringing such an extraordinary challenge.

The committee in the swine extraordinary challenge, however, did admonish the panels to stay within their proper role.

The third case, the lumber case, is ongoing and actually oral argument is scheduled in that case next week. All three cases involved agriculture or natural resource products. Two of the three, the swine and lumber case, dealt primarily with one important issue, this so-called specificity issue.

Now, the panels in the pork, swine, and lumber cases did not function in significant respects as the United States would have hoped, although I want to add to my written testimony that in the swine case, there have been follow-on cases dealing with subsequent administrative decisions of our department which we believe went better, but in those three cases, the system did not function in significant respects as we would have hoped.

In other respects, the binational panel mechanism generally is functioning as intended under the agreement. Panels reviewing final antidumping and counter——

Chairman LAFALCE. Why did they not function as you would have hoped? You are not talking about the outcome. You are talking about the process.

Mr. JOFFE. No. We are talking about the outcome. The panels read our law in a way that we disagreed with, and the Extraordinary Challenge Committee, under its criteria, did not accept our challenge, and we simply mean that the outcome was not in accord with——

Chairman LAFALCE. We lost?

Mr. JOFFE. With our views, correct.

Chairman LAFALCE. But we have no objection to the process; is that it?

Mr. JOFFE. We believe that on the whole the process is running properly. As you may know, in the lumber challenge, which is ongoing, one of the issues that we have raised before the Extraordinary Challenge Committee, which is to be heard next week, is a challenge to the composition of one of the panels. But again, the process——

Chairman LAFALCE. What was intended during the negotiations, Mr. Roh, with respect to utilization of the extraordinary challenge?

Mr. ROH. Well, it was set up as a kind of a safety valve in extraordinary cases, and if you look at it, there have been 30, 40 cases that have been decided by panels and three have been taken to extraordinary challenge, and in each—so I think that the—we followed that practice.

Chairman LAFALCE. What is the standard that we have used in those three cases to determine the propriety of pursuing an extraordinary challenge?

Mr. ROH. We have used the standards of the agreement which call—there are four or five standards there, and whether you think that what is going on here is so upsetting——

Chairman LAFALCE. Do you recall what those are?

Mr. ROH. I don't have them memorized.

Chairman LAFALCE. Mr. Joffe, do you have them?

Mr. JOFFE. Yes, I believe I can give that to you.

Mr. ROH. But one of the—a key element is that it isn't just an automatic appeal. I mean, you get into a court process and you would appeal, if you simply are the paying client.

Chairman LAFALCE. This is one of the most contentious of issues and I want you to expand upon it.

Mr. JOFFE. On page 3 of the testimony at the bottom, it indicates that an ECC can review a panel decision for gross misconduct by a panelist, serious departure by the panel from a fundamental rule or procedure, or for whether a panel has manifestly exceeded its powers, authority, or jurisdiction. Those are the criteria.

Chairman LAFALCE. We have applied those criteria in three instances, you say?

Mr. JOFFE. That is correct.

Mr. ROH. Mr. Chairman, you always look at a result and say, does this meet—is this result, if we are unhappy with it, does this meet the kind of standard implied in the agreement?

So, we have decided to take three cases to an extraordinary challenge, but it isn't that we haven't been asked or haven't considered it.

Chairman LAFALCE. I will explore this more during the question and answer period. Why don't you conclude your presentation, if you can, Mr. Joffe? Continue.

Mr. JOFFE. Yes. I think I can wrap up here shortly and I think what I was next going to say is responsive to your concern.

The experience of the Department of Commerce with panels generally has been that we do not win or lose more issues than we do in the domestic courts. Of the 15 panel decisions regarding United States agency determinations, 4 affirmed the agency's determination without remand. In other words, it was a total win without further ado.

Others, there may have been, in effect, a win after it was remanded and additional proceedings were held, but on balance, the results are about the same as we have in our domestic courts, and I cite here in the testimony, I wasn't going through it right now, a couple of instances in which panels decided issues in our favor that other panels had decided against us in the cases that I referred to a moment ago, simply to indicate to you that our experience has not been by any means uniformly negative.

Panel decisions, in addition, are not precedent for other panels or for courts, unlike——

Chairman LAFALCE. How many panel decisions have there been?

Mr. JOFFE. There have been 15 actual decisions. More cases may have been brought and withdrawn and so on, but there have been actually 15 regarding United States agency determinations.

Chairman LAFALCE. In how many of those instances was the position that the United States had initially taken upheld?

Mr. JOFFE. Of course there is a mix of issues. We won some and lost some. It is roughly the same as it has been in the courts, in our domestic courts.

There were these three that we cited that went all the way to extraordinary challenge. There were four that were flat out affirmed in our favor. In between there was a mix of issues.

These decisions, as I said, are not precedent for other panels or for courts, unlike our own court decisions, and it has been our experience that panels in fact, do not rely on other panel decisions as binding precedent.

So, given this record, we would not conclude that because we have had three extraordinary challenge cases, that the system somehow on the whole is not working.

As noted earlier, the panel process does have potential benefits. Of course it can be improved. We have worked to improve it as we moved from the CFTA to the NAFTA, and we are continuing to work on that, and we are committed to doing that as part of our implementation of the larger Free Trade Agreement which is greatly benefiting the United States as well as Canada and Mexico.

The administration is committed to a strategy of trade liberalization to boost U.S. economic growth. NAFTA and the Uruguay Round agreement are important elements of that strategy, along with our bilateral efforts to open markets around the world.

Through freer trade and more open markets worldwide, we can achieve greater U.S. exports and increased American jobs. At the same time, we will maintain the strength and effectiveness of the antidumping and countervailing duty laws, for which our Department has responsibility.

Liberalization of trade can only be sustained if it is not accompanied by unfair practices that undermine employment and competitiveness. As we work for the benefits of expanding trade, we remain dedicated to maintaining strong unfair trade laws, and vigorous enforcement of American rights under domestic law and international agreements.

Chairman LAFALCE. Thank you very much, Mr. Joffe.

[Mr. Joffe's statement may be found in the appendix.]

Chairman LAFALCE. Our next witness, Professor Murray Smith, director of the Center for Trade Policy and Law, Carleton University and the University of Ottawa.

Professor Smith.

TESTIMONY OF PROFESSOR MURRAY SMITH, DIRECTOR, CENTER FOR TRADE POLICY AND LAW, CARLETON UNIVERSITY, OTTAWA, ONTARIO

Mr. SMITH. Thank you, Mr. Chairman. It is an honor to appear before the committee and it is a pleasure to appear before you again.

I can recall some hearings that you held in Niagara Falls, New York, some years ago that I participated in.

When we were talking about this enormous Canada-United States bilateral relationship, I am struck by the fact there is prob-

ably more trade across bridges in your district than there is in many countries in the world.

Chairman LAFALCE. That is another reason for having this hearing.

Mr. SMITH. The theme of my testimony is that Canada/United States economic relations aren't broken, but we shouldn't take that important fact for granted.

There are some very strong pressures on the relationship and there are some serious outstanding problems, which if they are not serious efforts to resolve them, could have damaging repercussions.

Some of the sources of these pressures come from perception in one country or the other, but others stem because there is hard and difficult policy problems that the governments in the countries need to address.

I will dwell very briefly on the good news, which is, as usually is the case, is no news, and that is if we look at the overall relationship, it is not only an enormous relationship in economic terms, total flows of goods, services and investment income in excess of $250 billion, but it is also one that is remarkably balanced.

The U.S. Commerce Department, and I hasten to add I have used all my data from Commerce Department sources so we would have no disagreement on the panel about the numbers, indicate that the United States had a bilateral current account surplus of $1 billion with Canada in 1993. This is a remarkably balanced situation, especially when both countries have large current account deficits with the rest of the world.

Of course, if we go into the various categories of goods and services, there are different bilateral balances and surpluses and deficits in the various categories. The one point I want to stress though, in looking at the numbers on the relationship, is that as an economist, I conclude that the Canada-United States Free Trade Agreement from 1988 to 1993 worked well to the mutual benefit of both countries in stimulating trade and economic growth at a time when it was much needed amidst the prolonged recession of the early 1990's.

Just for example, U.S. exports of capital goods, this again is from Commerce Department classification, exports to Canada surged 50 percent from 1988 before the Free Trade Agreement to $30 billion, while similar U.S. exports to Europe during that period expanded only 20 percent.

On the other side, Canadian exports of capital goods to the United States surged $6 to $14 billion. So, as tariffs have come down under the Free Trade Agreement——

Chairman LAFALCE. If I may interrupt you there, since you used percentages with respect to the U.S. exports, it might be helpful to use percentages rather than dollar amounts, and so if you subtract the $6 billion from the $14 billion, that gives you a base of $8 billion.

So, $6 billion, to me, it sounds like a 75 percent surge for Canada, so Canada had a phenomenal surge, and I know that the agreement is probably criticized far more in Canada than within the United States, but when you compare the 75 percent surge in exports from Canada to the United States in comparison to their

performance with the rest of the world, do you know exactly what that was?

It seems to me they had a decline in their exports with the rest of the world, but I wouldn't bet on that.

Mr. SMITH. Well, Canada's trade with the rest of the world was weak in the late 1980's and early 1990's, partly because our dollar was strong, both against the U.S. dollar, but also because the U.S. dollar was strong. It was especially strong against offshore currencies.

So, we lost—had very slow export growth.

Chairman LAFALCE. I just wanted to make sure we were using apples and apples, and so I wanted to convert your——

Mr. SMITH. I guess in response to your point, I would look at it and say that manufacturing trade and capital goods have surged in both directions across the Canada-United States border, and that there hasn't been a large swing in the bilateral trade balance in either direction.

It has been growth in two-way trade across the Canada-United States border, and I think this is evidence——

Chairman LAFALCE. Which may be due in part to the floating exchange rate considerably strengthening American dollars, at least vis-a-vis Canada as opposed to, say, Japan.

Mr. SMITH. Certainly the exchange rate movements have significant influence on trade flows, but this very strong trend in the growth of manufacturing exports between Canada and the United States and its manufactured exports that were where the tariffs were being reduced the greatest under the Free Trade Agreement, that surge in two-way trade of manufactured exports suggests to me that it was both large enterprises and small enterprises are restructuring and specializing under the Free Trade Agreement, and that it may be related enterprises.

It may be one subsidiary of a multinational enterprise shipping to another subsidiary, but they are specializing in a variety of ways and taking advantage of the opportunities and responding to the competitive challenges under the Free Trade Agreement.

Unfortunately, we could explore the intricacies of that process in some detail. One of the political problems in Canada, however, is that public perceptions are not the same as those of economists or trade specialists.

For most Canadians, the implementation of the Free Trade Agreement was associated with this lingering recession of the early 1990's, and for many, it was a cause of the recession.

Another problem on perceptions is that the existence and persistence of these high profile trade disputes confirms their concerns that NAFTA, like the FTA before it, provides lopsided benefits to the United States.

It is interesting, there was a lot of debate about NAFTA here in the United States, but in Canada, opposition to NAFTA reflected more continued concerns about perceived vulnerability to the United States and much less concerns about potential Mexican competition.

The Canadian public seems to perceive every trade dispute as Canadians being harassed by litigious Americans, however, the specialists, both Canadians and Americans, have a relatively favor-

able assessment of the dispute settlement mechanisms under the Free Trade Agreement, which are continued under NAFTA.

In particular, among the specialist communities of the trade bar and academics in both countries, the Chapter 19 process has acquired credibility for providing fast and effective review of the administrative agencies according to the appropriate standard of judicial review in the domestic law of each country.

However, there is concern that the acrimony over the current softwood lumber dispute could undermine the credibility of this process.

One further point I would mention on dispute settlement, which is not reflected in my testimony, is there was mention earlier in the panel of the investor state dispute settlement mechanism which is new under NAFTA.

There is a looming issue in Canada which involves the issue of the use of trademarks for cigarette companies, which is linked in a sense to a response to the fact that the Canadian government has lowered cigarette taxes to reduce smuggling of cigarettes between Canada and the United States.

There is a risk that the first case that might arise under this investor stake dispute settlement process might arise with respect to whether the tobacco companies are receiving fair treatment with respect to their trademarks.

I won't say anything more about that, but that is obviously kind of an emotional and political issue that could generate some concern in Canada.

Turning to this issue of another problematic sector, the agrifood sector, unfortunately, an overall trade balance within the sector is not sufficient to assure harmonious trade relations.

Again, the Commerce Department shows that the United States exported $5.9 billion in agrifood products, and imported $5.6 billion in food and feed and beverages from Canada, but that has not made these contentious disputes in this sector any easier.

Those issues have proved difficult to resolve and I might be accused of a diplomatic understatement if I said that the recent tour of Latin America by the U.S. Secretary of Agriculture seeking to recruit countries to launch anti-dumping and countervailing duty cases against Canadian exports of wheat was seen as counterproductive in Canada.

How did we get here in agriculture trade issues?

Chairman LAFALCE. I know of one former Member of Congress who has some concerns about that too.

Mr. SMITH. In the Canada-United States Free Trade Agreement, the 27 countries agreed to remove tariffs and some nontariff barriers on bilateral agricultural trade, as well as removing export subsidies from bilateral shipments. But the tough problems, the quota restrictions on sugar, dairy, and peanuts in the United States, dairy and poultry in Canada, the domestic farm subsidies, the export subsidies on agricultural products into third markets, all were put aside to be dealt with in the Uruguay Round.

You might recall that the Uruguay Round was supposed to be concluded at the Brussels ministerial and both Canada and the United States were seeking global elimination of export subsidies

at that time which would have helped resolve many of our problems in this sector.

Unfortunately, however, the Uruguay Round was delayed and implementation will not start until 1995. In the meantime, these bilateral frictions have festered. Export subsidies, such as the U.S. Export Enhancement Program and Canada's WGTA, the Western Grain Transportation Assistance Act, will be reduced, but not eliminated by the year 2002.

Reflecting the concerns of dairy farmers who are concentrated in Quebec and poultry farmers, Canada is converting those import quotas into high tariffs under the agriculture chapter of the World Trade Organization, the WTO.

On its side, the United States is imposing tough restrictions on sugar containing and peanut products from Canada and is seeking now significant new tariffs on wheat from Canada.

Some U.S. farm groups perceive that Canada obtains lopsided benefits from the Canada-United States FTA agricultural chapter, which is now continued under NAFTA. The problem is that although the overall level of subsidies in most of the key commodity groups are similar in the two countries, and in some cases Canadian subsidies are much lower, differences in the structure of the farm programs, the administrative arrangements, how those programs are delivered, all of these differences are sources of perceptions of unfairness.

The Uruguay Round rules for agricultural subsidies are a useful and important step, but only a step toward resolution of these problems.

In addition to these continuing problems over agricultural subsidies, this commitment to deal with the unfinished business of the Canada-United States Free Trade Agreement was not included in the same form in NAFTA. However, as we have already discussed this morning, the new Canadian government, the liberal government, when it came to power last fall, with some ambivalence about NAFTA, indicated that completing this unfinished business under the Free Trade Agreement was a very high priority for them, and they sought and, in their view, received very strong assurances from the U.S. administration that a working group would deal with these issues over 2 years before Canada decided to proceed with the implementation of the NAFTA on January 1st.

Now, how are we going to deal with these difficult issues? In my view, the Uruguay Round and the WTO and its related agreements provide a very useful basis for dealing with subsidies and countervailing duties in a North American context.

On contrast, however, the antidumping chapter of the WTO, if implemented faithfully, will have very modest impact upon the application of antidumping laws within NAFTA. I must hasten to add, however, that there is great concern in Canada, both in the private sector and within government, that the Uruguay Round implementing legislation in the United States will seek to exploit any ambiguity in the international arrangements in order to create a more protectionist regime for antidumping and countervailing duty laws.

The Canadian Government is committed to making progress on the unfinished business under the FTA and NAFTA as is evident from the recent speeches by the Trade Minister, Roy MacLaren.

In my view, the most obvious focus for further work is on the application of the antidumping laws, because it may be difficult to go much further with respect to subsidies and countervailing duties than is achieved in the WTO, and because the removal of tariff and nontariff barriers within the NAFTA over time changes the rationale for antidumping laws.

Although the Chapter 19 process seems to have worked relatively well, I think all sides would agree that judicial review under the existing laws is not and ought not to be a substitute for—it was not intended to be a substitute for better and more clearly defined trade rules.

In conclusion, good faith implementation of the Uruguay Round is a necessary, but not a sufficient condition for maintaining mutually beneficial trade and economic relations. Canada and the United States will need to demonstrate goodwill in order to avoid any negative fallout from the softwood lumber dispute.

They will need to work harder to resolve outstanding bilateral agricultural trade and subsidy issues, and must make greater effort to find common approaches to the application of trade laws, especially antidumping laws within NAFTA.

Policy-makers need to keep in perspective the overall balance in this enormous relationship and keep in mind the mutual benefits to be derived from building upon the present level of cooperation.

Thank you.

Chairman LAFALCE. Thank you very much.

[Mr. Smith's statement may be found in the appendix.]

Chairman LAFALCE. I have many questions, but I asked a number during the course of your testimony. So, I will call upon the other Members first.

Mrs. Meyers.

Mrs. MEYERS. Thank you, Mr. Chairman.

I wonder, Mr. Roh, or—well, any of you really, tell me about the makeup of the panels. How are they appointed or elected, how many members are there, if there are two countries involved in a dispute, are they from the two countries involved now that NAFTA is in existence, do they have to be from all three countries? Tell me about that.

Mr. ROH. Sure. The panels are constituted from private sector experts that are usually out of a roster, and in a bilateral dispute, this—we will talk about Chapter 19, these panels that were using subsidy and dumping determinations. Two would be from the United States side, two from the Canadian side, and the third would be chosen—there is a complex system.

If the two—if the four panelists aren't able to agree, then—at the end, it can be bilat in short, so you have got a 50/50 chance of three Americans or three Canadians.

Where there is a trilateral dispute, under Chapter 19, all disputes are bilateralized, if you will, so that doesn't come up. If you have a three-way dispute in—under the terms of the NAFTA, that is, suppose it is a dispute about whether or not your quota is legal and two of the countries are complaining about the third, then the

defending country is assured that at least two—of picking at least two, and the plaintiffs have to—are assured only of picking one each, and the fifth can be either from the defending country or from—chosen by the defending country or by one of the complaining parties.

It is to give a little extra assurance to the country whose practices are on the lot—are on the line, that it won't be subject to a ganging up, if you will.

Mrs. MEYERS. Who chooses them from this roster?

Mr. ROH. The governments.

Mrs. MEYERS. I beg your pardon?

Mr. ROH. The governments.

Mrs. MEYERS. Is that your office then or Commerce?

Mr. ROH. It is——

Mrs. MEYERS. Commerce would choose them?

Mr. ROH. Yes. We tend to have harmonious relations though, within the government.

Mrs. MEYERS. We might be interested in some more information about how that fifth panelist is picked and how—you say it is a complicated process, but we would like to know in the past, how has that worked and has it been contentious?

Mr. ROH. It has always been bilat. We have all these complicated systems, but it just ends up easier doing it bilat.

Mrs. MEYERS. In other words, both groups agree on a number of people who can go into the fifth panelist, and it is drawn or how is the bilat——

Mr. ROH. Bilat, you decide which country picks the fifth panelist.

Chairman LAFALCE. Can I ask a question?

Mrs. MEYERS. Yes.

Chairman LAFALCE. Looking back over those instances when the fifth panelist has been the deciding vote, well, there have been, what, 15 decisions, did you say?

Mr. ROH. Yes.

Mr. JOFFE. At the panel level, right.

Chairman LAFALCE. At the panel level. How many of those 15 have been, 3 or 2?

Mr. ROH. One.

Chairman LAFALCE. Only one?

Mr. JOFFE. Virtually all the decisions have been unanimous.

Chairman LAFALCE. All right, fine.

Mrs. MEYERS. We have lost—well, three have gone to an extraordinary, and four we have won, so that means that we have lost eight?

Mr. JOFFE. No. In the remaining ones, we may have won part and lost part. In four it was a total win without remand.

Mrs. MEYERS. I see. So, on those remaining eight, we may have won a portion of the dispute?

Mr. JOFFE. That is correct.

Mrs. MEYERS. And lost——

Mr. JOFFE. It tends to be about the same as our win/loss ratio in the courts.

Mrs. MEYERS. Mr. Joffe, when the panels review U.S. law, how do they view the legislative intent and history? Can we do something to clarify our laws, our intent?

Are we going to have to change the way we develop our laws now that they are subject to this kind of scrutiny from—by these panels?

Mr. JOFFE. They are supposed to be looking at our law and interpreting our law according to the same criteria that a court would use, and so legislative intent would be relevant.

In some of the cases, we are actively looking at the question of whether there are issues that we would propose to Congress that should be further clarified simply so that a subsequent panel would have—there would be no doubt, no ambiguity on some of the points that have caused difficulty.

So, there is a way that, through further enactments of the Congress, these matters can be further clarified and emphasized.

Mrs. MEYERS. I think this is an area that we are going to have to be looking at as we develop our own laws, not only because of these panels with NAFTA, but because of the World Trade Organization, and I think some people perceive that there is going to be a threat to our sovereignty in the World Trade Organization.

It means we are going to have to be very cautious about how we have to—how we develop trade law and how we develop our intent and the background with which we develop trade laws, environmental laws, labor laws, because they are going to be subject to a different kind of review than they have been in the past.

Mr. JOFFE. May I just add that the situation with the panels under NAFTA in that respect is very much the same as the situation with respect to our domestic courts.

That is to say, there is a dialogue between the Congress and the courts where, if the court rules in a way that Congress believes was improper, did not properly reflect the legislative intent, then Congress may go back and reemphasize, clarify, so that there will be no doubt.

Mrs. MEYERS. Finally, I know that one of the most contentious problems between Canada and the United States, at least to my awareness, has not been suds or spuds or hogs or logs, but it has been wheat, and has that problem been resolved and where are we in that dispute?

Mr. ROH. That dispute is—or that issue has not been resolved. That wheat along with, as the Chairman noted, dairy, poultry, sugar, sugar containing products, and peanut products, those are all products that in some senses were affected by this combination of the Uruguay Round rules, which took one approach, and the NAFTA and CFTA, which took another and have—what we are trying to do is work out a solution.

I mean, each of them has to be solved on its own merits, but they all do have to be solved, and in fact, my boss, Ambassador Kantor, as well as Secretary Espy will be meeting with their counterparts toward the end of this month in a further effort to resolve that matter.

Mr. SMITH. If I just might comment on the wheat issue. This issue has become very contentious in Canada, and I think it is an area where we have to keep in mind the long-term goal.

I think both Canada and the United States share the long-term goal of reducing export subsidies on a global basis, but what I found puzzling about the Agriculture Secretary's particular initia-

tive against Canadian offshore wheat exports is that if Canada were to stop tomorrow our export subsidies, which amount to about $15 a ton, where U.S. wheat runs 50 to $60 a ton, United States, it varies from sale to sale, the immediate effect of Canada stopping its subsidies tomorrow, as long as the EEP would be there, would be that there would be more pressure for wheat to come across the United States-Canada border instead of going across international markets.

So, the way this issue is managed will require some sophistication and recognition that we need a long-term goal, but we need a sensible way to get to that long-term goal.

Mrs. MEYERS. Do you think that the general agreement on tariff and trade, inclusion of agriculture, is going to help resolve this problem between Canada and the United States? Will it make it more contentious?

Mr. SMITH. In my review, the Uruguay Round rules on agriculture have helped resolve it, but they help in the longer term. The problem is how we get there from here, that the Uruguay Round doesn't get us global free trade in agriculture; it gets us somewhat free trade in agriculture in the next century, and it helps, but it doesn't solve the problems about how we deal with these contentious export subsidy issues or the contentious domestic subsidy issues between Canada-United States in the agricultural trade, and I think that is the problem.

We have to recognize that we need to go further and build on the Uruguay Round results in the area of agricultural subsidies and trade barriers if we are going to have a constructive resolution of these issues in North America.

Mrs. MEYERS. Well, I have more questions, but I will submit them to the panelists. I don't want to take more than my time and I want to say, I think this was an excellent panel and an excellent hearing.

Thank you, Mr. Chairman.

Chairman LAFALCE. Thank you very much. As a tremendous consumer of pasta, I am very interested in this debate. We will return to this issue later.

Mr. Conyers—Chairman Conyers.

Mr. CONYERS. Thank you, Chairman LaFalce, and good morning, gentlemen. I am delighted to have heard most of your comments.

My interest derives out of the fact that I represent Detroit on the border, the Canadian border, and the automobile industry has great interaction between both countries, and so I want to raise that the—your analysis of where our relationship in the automobile industry is going in terms of how both countries see it, as well as the corporations, and I am also concerned about some of our environmental agency regulations which may be subject to challenge under our trade agreements, particularly with asbestos where there have been Canadian challenges to EPA's attempt to phaseout the production and importation of asbestos.

So, in those two general areas, I would like each of you to make some summary remarks, please.

Mr. ROH. Well, Mr. Chairman, I will take a stab. On the auto side, as you know, as you well know, we have had a tremendous relationship with Canada.

We have had free trade since 1965 with—or a substantial removal of barriers. There is some irritants that—a few irritants that remain, I suppose, on both sides, but basically we have an integrated market between, and an integrated production between the United States and Canada and that has been, I think, a beneficial relationship, not free of—completely free of dispute.

I think in the NAFTA, we actually made some improvements in the United States-Canadian relationship, as well as by adding Mexico, among other things. Of course the rule of origin was made stronger, it was made clearer.

It now is 62.5 percent rather than 50 percent, and so some of the old bones of contention were eased between the United States and Canada in that agreement.

On the environmental side, there was something of a myth that the asbestos issue was a function of the trade agreement. In fact, under our own legislation, there is no private right of action. You can't sue in court as a private citizen to complain about a violation of the trade agreement.

The environmental groups were complaining about a violation of U.S. law, and that is why they went to U.S. court.

We have retained the right to establish and maintain our own environmental standards, to raise them and so forth. So, I don't think you need to be worried that we will be sacrificing environmental quality.

Indeed, I think the intent of the United States and Canada and Mexico is to raise, rather than—or improve those environmental standards, rather than lower them. Certainly there is nothing in the trade agreement that calls for lowering them.

Mr. CONYERS. So the environmentalists are over excited on this question? Not to worry, is that the message?

Mr. ROH. We retain our ability to establish our own environmental laws. I think I will let the first part of that question slide, if you don't mind. But we retain our own ability to set our own environmental standards.

Mr. CONYERS. Very good.

Mr. JOFFE. I have just been advised that our information is that exports of automobiles from the United States to both Canada and Mexico, especially to Mexico since implementation of NAFTA, that preliminary indications are that they are significantly on the rise.

Mr. SMITH. First of all, Mr. Chairman, as a personal note, I am an alumni of the University of Michigan so I am quite familiar with the immediate context of your district.

On the automotive trade, I think this has been a tremendous area of cooperation between Canada and the United States for decades. I think in their own way, both the Free Trade Agreement and the NAFTA have served to resolve a number of the outstanding problems or irritants between Canada and the United States.

I don't think the auto pact as we knew it before the Free Trade Agreement would have survived to the present without the kinds of changes that have occurred through the Free Trade Agreement and the NAFTA.

I think that the——

Mr. CONYERS. Why is that?

Mr. SMITH. I think there would have been real pressure, perhaps more on the United States than Canada, but some of the aspects of Canadian policy that were changed as a result of the Canada-United States Free Trade Agreement and the NAFTA, such as, for example, the duty remission arrangements that Canada had negotiated with the Japanese automotive assembly companies. Canada took the view that was permitted under the auto pact.

There were less sanguine views. I think the current Ambassador of the United States to Canada, was formerly the governor of Michigan, had some concerns about the longstanding Canadian policy in this area, and those provisions have been changed or are in the process of being changed as a result of both the Free Trade Agreement and the NAFTA.

I also think, as Mr. Roh has indicated in his testimony, that some of the administrative issues and problems that arose with respect to the rules of origin under the Canada-United States Free Trade Agreement have been addressed through the North American Free Trade Agreement.

It is not clear to me that they have been simplified, but the administrative—preexisting administrative problems have been—to considerable extent been clarified and been made more precise through the NAFTA.

So, I think what we have done is build on the history of cooperation in this sector, and I hope we will continue to build on the history of cooperation in this sector.

Mr. CONYERS. So dispute resolution is the main problem that we are discussing here today and as you three see it, is the main problem that we have to consider in terms of our relations and the agreements?

Mr. SMITH. Well, let me just respond to that. Perhaps—echoing what Mr. Roh said earlier, that I think that in a number of areas, what really matters is that the governments and in conjunction with the legislative branches of the parliament in Canada, the Congress in the United States, are able to work out and resolve these issues.

It is only when the governments are unable to resolve the problems that you are forced to go to a dispute settlement mechanism, and I think the dispute settlement mechanisms can be useful in the context of an intense and complicated relationship like that between Canada and the United States, but we have to be careful.

I must plead a special interest here. I am involved in a dispute settlement panel right at the present time. I think it is unfair to expect that the panels can solve all the problems. I think it has to be ultimately the governments and the bodies politic of the countries that have to resolve these issues, and I would say that in the automotive sector, there has been only one—a very small issue that went to a panel under the Free Trade Agreement.

The issues that have been resolved in that sector have been resolved through the negotiation process and through the implementation of international agreements. So, it has not been through the dispute settlement process in that particular sector.

With respect to the environmental challenges, I think the trade and environment issues are ones we are going to have to deal with for decades to come, but I would agree with the comments made

earlier that the NAFTA certainly does not circumscribe the ability of Canada or the United States to set environmental standards.

I think all of us will find it an interesting adventure in terms of our work with the North American Commission on the Environment, and I think it could well—I am optimistic that it will lead to very effective cooperation in the environmental area among the three countries.

But again, that is something that works best if the governments can effectively cooperate rather than simply relying on the dispute settlement process to solve the problems.

Mr. ROH. I think, Mr. Chairman, we agree with—I agree certainly with Professor Smith that dispute settlement isn't the big problem in the relationship. You need a dispute settlement mechanism where you haven't been able to negotiate it out, but it is just like any group of people or businessmen, you are so much better off if you negotiate a solution than if you have to turn it over to a panel, but you need that mechanism partly to encourage you to achieve the negotiated solution.

As I look back on the last half dozen years, overwhelmingly, we solved things by negotiation, and rarely do we have to end up in dispute settlement on these cases.

Mr. CONYERS. Well, I thank you very much.

Thank you, Mr. Chairman.

Chairman LAFALCE. Thank you.

Mr. Torkildsen.

Mr. TORKILDSEN. Thank you, Mr. Chairman, and I also thank the witnesses for their testimony today.

The only question I would like to add, because the witnesses covered quite a few already, is to ask about the general benefit that you see through NAFTA so far, and would that continue with GATT? Can you just give us your own thoughts on where you think we would be if NAFTA did not pass?

I know you can't say with certainty, but could you just envision for us what may have happened if NAFTA had been defeated?

Mr. ROH. That sounds like a question for Professor Smith. Awfully hard to speculate on that. I think the passage of NAFTA sent a very positive signal for the conclusion of the Uruguay Round negotiations and for the President as he went to the Pacific, but as to what would have happened, I think it is very hard to guess what happens if you don't conclude the NAFTA, and happily we don't have to guess at that.

Mr. SMITH. I think it is much better that we are not in that situation because whatever your views on the merits of NAFTA, I think if it would have been rejected last fall, it would have created a very problematic dynamic between Canada and the United States.

I think there is a current disposition with the current government of Canada that was elected last fall to seek warm relationships with the United States, but also to have an independent approach to foreign policy, so I think the Canadian government might have quickly responded to a United States rejection of NAFTA by going ahead bilaterally with Mexico. Probably they would have done it in good faith and said, OK, when the United States is ready to come along, come along because I think that—the potential dy-

namic of that very hypothetical situation could have been quite unpleasant.

I think what I would perhaps focus on is more to the issue of what will happen with respect to Uruguay Round implementation. I think we have got some problems, Canada-United States right now. I think those are manageable. The Uruguay Round only helps solve them. It doesn't solve them completely.

But if the Uruguay Round implementation fails or if it is viewed in Canada or in other countries as implemented in a way as to—the pill is not sugarcoated, but is—has contained some hooks and riders which are viewed as very troublesome, then I think we will be in a much more difficult situation to manage.

So, I think that is an issue that is ahead of us rather than the NAFTA issue, which is behind us.

Mr. TORKILDSEN. If the GATT round does not clear the House, would the United States ability to negotiate any trade agreements be severely hampered?

Mr. SMITH. I think having—certainly the rejection of any trade agreement by the United States Congress, given all the effort that the—any administration puts into the negotiation of that agreement, all the consultation that takes place between the administration and the Congress, if it is ultimately rejected by the Congress, that sends a very disturbing signal to trading partners.

That would be even more disturbing in the context of the Uruguay Round because it is not just a bilateral negotiation, it is the global system that is at stake, and I think it would have quite profound consequences on how other countries, including Canada, would view the ability to conduct trade or international economic negotiations generally with the United States.

Mr. TORKILDSEN. Thank you, and, Mr. Chairman, I want to thank you for holding this hearing because I think it was very helpful.

Chairman LAFALCE. Thank you very much. When I first came to Congress, I was usually impressed with the cataclysmic arguments that were offered by those that, if you do not do this, the world will fall apart.

Having been here a few years, I am less and less impressed with that line of reasoning. What would happen to Canada if the Bloc Quebecois became the opposition party? Life goes on. Life goes on.

Do you have any questions?

Ms. MARGOLIES-MEZVINSKY. No.

Chairman LAFALCE. All right. Then let me ask a few questions.

When we adopted the FTA, we did call for a phase-out of all tariffs over a 10-year period. That is mandatory, but we also had a timetable. We had different schedules, but we also hoped for an acceleration of the phase-out above and beyond the timetables.

How has the acceleration process been going as opposed to the prescribed process?

Mr. ROH. Mr. Chairman, the acceleration process has worked very well. We had three rounds of tariff acceleration negotiations with Canada to date and we have a fourth one in train.

So, far we have been able to speed up the process of elimination of duties on some $9 billion a year in two-way trade. So, that has been very heartening, and that has been—I should note that the

sort of informal ground rules have been, we proceed to accelerate where there is no material opposition on either side.

So, this represents taking a rather conservative approach to the negotiations, it was still some $9 billion in trade where we have been able to actually go faster than originally projected.

Chairman LAFALCE. Any other comments? The trade minister, Roy MacLaren, was here a few weeks or so ago. I met with him, Rufus Yerxa, et cetera. Subsequently he met with Mr. Kantor.

There have been statements made that I read in the press about improvements in the dispute resolution mechanism process. I don't think I heard from you anything that may be under discussion right now.

Has anything been made public as to what these improvements might be?

Mr. ROH. I will take a first stab and perhaps my colleagues want to add something. We are at the start in that exercise, and in fact, one of the things we are looking for is input from our respective legislatures and from the private sectors of both countries as to what kinds of things would constitute an improvement.

It is very easy to be frustrated with the current system, and it is easy to pick at it, but——

Chairman LAFALCE. I am not frustrated with it at all. I think there are always going to be disputes and that is why we set out the panel system and it is working. It is working.

I have some questions about the resorts to the extraordinary challenge which we will delve into a bit more.

Mr. ROH. I meant it more in the sense that Winston Churchill referred to democracy, it is the worst system in the world except for all the others. One of the real problems we face is, can we do something that is an improvement on the status quo.

I think in any dispute settlement mechanism, you used to term that, I have sometimes used it in the past, when you lose, it is a nasty system or one part of your soul can't help that, but it is quite correct that back in 1987 and 1988 when this was being negotiated, it was viewed as sort of a provisional system with the thought that we would be able to devise a better regime.

Chairman LAFALCE. Let's get down to the critics. One of the advantages of the dispute settlement mechanism is it does take it out of a political context too, in addition to taking it out of a judicial context, quasi judicial, which is an expedited process. Is the extraordinary challenge in the American experience one that is based upon primarily legal considerations or primarily political considerations?

Is the extraordinary challenge now being viewed by America as a political escape valve?

Mr. ROH. No. I think it has been—I think we have used it quite properly, that is, when—if you look at the decisions, and the last one——

Chairman LAFALCE. Let's look at each of the three instances and juxtapose the reason we advance as against the reasons articulated in the agreement for exercise of that option.

Mr. ROH. You may have to call on Steve Powell for more precise——

Chairman LAFALCE. Is he here?

Mr. ROH. Yes, he is here. But let me note, I recall vividly the first one, it was an ITC decision, I believe, and the ITC complied, but made it very clear that they regarded the panel as having misapplied U.S. law, misstated U.S. law, invented its own law, and the decision almost tracked the terms for which an extraordinary challenge is required.

I would note, Mr. Chairman, that this mechanism was set up as a safety valve and it is not supposed to be an automatic appeal, and it hasn't been used for that purpose.

I think if you look at the last decision, it was, I believe, a 3 to 2 decision, a rather strongly worded dissent, split on national lines, indicating that U.S. law had not been followed.

Chairman LAFALCE. In the three instances, requiring extraordinary challenge, what has the vote been at the panel level?

Mr. ROH. I suspect it was unanimous in the first two cases simply because almost all of them were unanimous up to the point——

Chairman LAFALCE. Was it Mr. Powell?

Mr. JOFFE. Mr. Powell is the Chief Counsel for Import Administration.

Mr. POWELL. The vote was unanimous in the first two cases and it was 3 to 2, a very close——

Chairman LAFALCE. In the first two cases. What were the first two cases, Mr. Powell?

Mr. POWELL. Pork and swine.

Chairman LAFALCE. So it was 50/50, and in the pork and swine cases, what were the justifications for seeking——

Mr. POWELL. Well, Mr. Chairman, in all three cases, the basis for the United States challenge has been that the panel did not apply the appropriate standard of review, not that we lost or won.

Chairman LAFALCE. Did not apply the appropriate standard of review. Now, that differs from an inappropriate interpretation of the law?

Mr. POWELL. That is exactly right.

Chairman LAFALCE. What is the appropriate standard of review that should be applied and what was the inappropriate standard of review, in our judgment, that was applied?

Mr. POWELL. Basically the courts are required to apply the same standard and the panels are required to apply the same standards of the courts, and that is a substantial evidence standard which requires, as under the Supreme Court Chevron decision, substantial deference to the administering authority, and in effect, we argued that the panels had not accorded to the expert administrators of the law the proper deference to their findings on the facts and to their findings on the law, and that is the basis for——

Chairman LAFALCE. Do you defer to administrators with respect to their findings of facts and their interpretations of law, or do you not defer to the administrators only on their findings of fact as opposed to their interpretations of law?

Mr. POWELL. Your Honor—Mr. Chairman, the difference——

Chairman LAFALCE. You may call me Your Honor.

Mr. POWELL. There is, you are right, a difference between the amount of deference that should be given to an agency on facts versus law, but even as to law, as long as the agency's interpretation is among those that are possible, that are reasonable interpreta-

tions of the congressional intent, the courts and panels should defer to that interpretation.

Chairman LAFALCE. What case law is there for that?

Mr. POWELL. That is based on a long line of cases beginning with Chevron, Your Honor—Mr. Chairman.

This is basic U.S. law that deference is—you start with the proposition of what did Congress explicitly require. If Congress is silent on a particular issue, then the agency must speak to the congressional intent, what would Congress have done in that instance.

Chairman LAFALCE. I have always interpreted U.S. laws to say that we defer findings of fact, but not to interpretations of law, but at least I now know what the basis was in those two instances. What was the basis in the 3, 2 case?

I believe that was the lumber case, was it not?

Mr. POWELL. It is essentially the same argument. We are saying that—not that the panel was correct in upholding us or not upholding us, but that they did not follow the standard set out in the treaty for the review of our determinations, and that is what the extraordinary challenge is supposed to be about.

Chairman LAFALCE. We cannot refer to it as a treaty because if we refer to it as a treaty, it would have required two-thirds vote of the Senate, and some individuals are saying that the GATT, creating the WTO, is, in fact, a treaty, and therefore must receive two-thirds concurrence of the Senate as an attempt was made after World War II, similar to the WTO, when the attempt was made to go to the Senate as opposed to a simple majority of both bodies of the House.

But go ahead. I just wanted to——

Mr. POWELL. Well, Mr. Chairman, the basis for lumber essentially is the same kind of underlying basis for challenging the other two decisions, that the panel did not apply the standard of review that a court would have applied in that same instance.

Chairman LAFALCE. All right. There was some discussion about a follow-up meeting between Mr. MacLaren and Mr. Kantor. There is even some discussion about having it in Niagara Falls.

Have they yet decided to meet again?

Mr. ROH. As I was noting on the agricultural disputes, they are going to be meeting at the end of June, and I think the last detail may not have been worked out. That would be also with the Secretary of Agriculture, Mr. Espy, and with the Canadian agricultural minister, Mr. Goodall.

Chairman LAFALCE. All right. As much as I praise the Canadian/American FTA, I thought there were problems with it. One of the problems was the glaring omission of dealing with subsidies, and another one had to do with the failure to deal with the exchange rate relationship.

Now, what was exchange rate circa January 1989? Does anybody recall that? I don't have it at my fingertips.

Mr. ROH. I don't have it at my fingertips. I remember more vividly the exchange rate when we were negotiating because I had to pay it.

Chairman LAFALCE. What was it then?

Mr. ROH. About 70 cents on the Canadian dollar it seems to me in 1987.

Mr. SMITH. The Canadian dollar peaked at 88 cents United States in 1981.

Chairman LAFALCE. It is now about what, 72 cents?

Mr. SMITH. Yes.

Chairman LAFALCE. That is a considerable swing from 1991 to the present. That is the point I was getting at, and that was the point I was getting at in 1986, 1987, and 1988 when I said you cannot have a Free Trade Agreement unless you address the issue of currency stability.

That was an issue that I raised. I mean, nobody would enter into a contract to be exercised 3 years from now agreeing to pay a certain dollar amount in Canadian money, German money, what-have-you, unless they dealt with that issue.

Yet we enter into trade agreements not dealing with that issue. Well, I was pleased in April of this year when there was a joint statement by our finance ministers and central bank governors of Canada, Mexico, and the United States that they would create a North American financial group to establish a forum for consultations and economic and financial developments, including, I think, a foreign exchange swap facility and above and beyond the swap facility, perhaps discussion on each other's currency levels.

Could anybody expand upon this? What gave rise to this agreement? Has anything happened since April of 1994, and although we have had a swing from 88 American cents to the American dollar to about 72 cents, the swings between the U.S. dollar and the Mexican peso have been a thousand times more volatile. Does anybody know what is going on there?

Mr. ROH. You would be much better off getting somebody from the Department of Treasury. Actually, let me take up a point about the peso. In fact, since 1989 it has been—it has been a very stable exchange rate.

Chairman LAFALCE. I understand.

Mr. ROH. It was very volatile in the 1980's.

Chairman LAFALCE. What is it since the uprising in Chiapas, Mr. Roh?

Mr. ROH. To the exchange rate?

Chairman LAFALCE. The U.S. dollar and the Mexican peso, yes.

Mr. ROH. It has stayed stable. Among other things, I suspect this swap and the expression of confidence in the stability of the peso probably contributed to that.

Chairman LAFALCE. I think that is something that people from USTR and Commerce should be concerned about also. I mean, it is so related to what your interests are.

There is no question that it has a profound impact on cross border trade. There is no question it has a profound impact on cross border traffic.

I am especially interested too, not so much out of the Canadian/American or the NAFTA relationship, but out of the United States-Japanese, United States-German relationship that Paul Volcker, within the past month or two, has called for a reconsideration of the Brenton Woods agreement and the possibility of a floating exchange, but within certain target zones, and I think that as we increase our international trade, as we go from the FTA to the NAFTA to the GATT, the imperative of dealing with exchange

rates' stability is greater and greater and inextricably interrelated to commerce and trade. So, I just wanted to make that point.

Professor Smith raises an intriguing question. He may not have made it with specific reference to the issue of subsidies, but we shortly will be receiving legislation from the administration for the implementation of the GATT.

That is going to be another controversial issue. Unlike the NAFTA where business was preponderantly in favor and labor was vehemently opposed, we are receiving mixed messages from those two camps. Although labor is primarily opposed and business is primarily in favor, their voices are not as strong for and against, and there are mixed voices. But I am interested in how the GATT is going to impact upon the NAFTA because the NAFTA has subsumed the FTA. I suppose this depends in part upon the implementing legislation.

Does anyone care to comment on that?

Mr. ROH. Sure, Mr. Chairman. The agreements are complementary. Basically the NAFTA goes further to—than the Uruguay Round in almost every respect to liberalize.

So, where the Uruguay Round cuts tariffs, with the NAFTA partners, we are eliminating them. But there is no inconsistency there. The GATT contemplates, as you know, as will the WTO, these free trade areas going further for countries agreeing to do so.

So, we don't see that there will be any incompatibility at all between the new—the Uruguay Round agreements and NAFTA.

Chairman LAFALCE. What would the dispute resolution mechanisms be under the GATT?

Mr. ROH. The GATT mechanisms are quite similar to those of the NAFTA. In fact, in terms of—where the dispute is over the terms of the agreement, both of them use panels and in both instances, a panel will make a decision that is not—I am not talking about Chapter 19 here.

I am talking about the more normal kind of dispute settlement in trade agreements as exists in the WTO. A panel's decision isn't binding in the sense that you can't be forced to change your law or change your regulation or change your practices.

The same is true in a NAFTA panel, as it was true in a CFTA panel. You can't be forced to change, but the aggrieved party will have—ultimately can have the right to retaliate if that party remains aggrieved by a practice that hasn't been changed, and the two agreements are quite similar. If we have a dispute——

Chairman LAFALCE. Well, Professor Smith expressed some concerns in his testimony that in our implementing legislation, when we deal with the measures we can take, countervailing measures, antidumping measures, that we do not authorize measures there that in some way would be violative of the FTA as subsumed by NAFTA.

Do you want to expand upon what you meant, what your concerns were, Professor Smith?

Mr. SMITH. Well, I can't respond in detail. I know there is great concern in Canada. I was reporting a perception in the sense, and it is a sophisticated perception, both across the private sector, within the Federal and provincial governments in Canada, who are seeking to track the implementing legislation.

I believe Mr. Joffe said that there was some dialogue with Canada and other countries on this issue, as well as interested parties in the United States.

I think one of the challenges is that because the way the fast-track process operates, it is hard to know exactly what will be in the ultimate implementing legislation until the administration is about to table that legislation.

I think that the problem is that there are many technical changes that might be associated with the antidumping and countervailing duty laws as part of the implementation of the Uruguay Round, and I suppose the challenge is, there may be 50 changes and there is a tendency to say, OK, which of these 50 is the most protectionist, and then you say, OK, well, we will take that number 50 off the list, or number 1, which is the most protectionist, but there is still a concern that the other 49 changes may, on balance, have an effect of making the enforcement of the laws more protectionist in their application.

So, I am saying there is a lot of concern on this issue.

Chairman LAFALCE. There is always a concern whenever you are going to adopt a new trade law that is multilateral in scope. There is always a concern that it might supersede through unilaterally implemented legislation what has been previously approved at a smaller multilateral, trilateral, or bilateral level.

Now, one way to deal with that is you are very careful about the language. But another way is to simply exempt previously agreed upon free trade agreements and say they stand on their own, they don't come within the embrace of the subsequent broader legislation.

Are we envisioning a submission of GATT legislation which exempts the NAFTA, exempts the signatory countries to the NAFTA?

Mr. ROH. Mr. Chairman, we will make sure that whatever we submit is fully consistent with all our international obligations.

There is a cottage industry in speculating—around the world in speculating that the United States might have some nefarious trick up its sleeve. I might say that we worry a lot about what our trading partners are up to. Most of them don't specify in detail. Instead they give themselves broad authority to violate the agreements instead of making it explicit.

But in the end, after all the worry, I think we submit legislation that is consistent with our international obligations.

Chairman LAFALCE. Let's get a bit more specific now. We, for the period of January 1989 through the present, stated that the reason that we were not doing anything to negotiate subsidy arrangements between the United States and Canada was because this was being discussed pursuant to the Uruguay Round.

Now, what are the subsidy provisions of the GATT that will be applicable to United States-Canada trade?

Mr. JOFFE. Mr. Chairman, the Uruguay Round actually contains a number of provisions strengthening our remedies and the restraints on subsidies. For instance, there is—if a certain amount of subsidy is given, there would be a presumption of adverse trade effects.

Certain presumptions would kick in. For the first time——

Chairman LAFALCE. Would you give me some examples of subsidy provisions within GATT that would have specific applicability to Canadian/American trade? Any examples in pork, swine, lumber or wheat?

Mr. JOFFE. Well, in any commodity or product, there are provisions in the new Subsidies Code that the Congress will be asked to implement which would apply to all of these things if certain—there are certain new strengthening provisions that would create presumptions that would make it easier to bring subsidy complaint to the WTO that would provide for the first time what we call disciplines, in the jargon of international trade, on competition in third countries.

So, for example, if one of our trade rivals is subsidizing products which are competing with our exports in other countries around the world, for the first time, because there would be teeth in the dispute settlement process, we would have recourse to stopping those subsidies and that unfair competition elsewhere in the world when we really had no such recourse before.

Our own countervailing duty actions in the more traditional area of imports into the United States would be facilitated by the fact that the new subsidies code incorporates many United States countersailing duty methodologies.

Chairman LAFALCE. Maybe not now, but at some point, I am going to need a more specific response so it is clear for me.

I mean, I remember we keep saying, we have to beef up Eximbank, otherwise it is unilateral disarmament, especially against the French? Is the GATT going to affect that? Are the GATT provisions on subsidies going to affect any of these issues in controversy between the United States and Canada? If so, how so?

Mr. ROH. Mr. Chairman, the GATT rules——

Chairman LAFALCE. Do the GATT rules define subsidies generically, or do they just list a specific set of practices that exist around the world and then say, these fall into the camp of subsidies and these don't?

Mr. JOFFE. There is greater definition than we have had before in the code as to what is a subsidy. That is another one of the achievements that was obtained in the round, yes. They are more clearly defined.

It will be easier to bring successful actions, and there will be increased remedies around the world.

Now, you ask whether this will obviate some of the tools that we have felt we have needed in the past. We certainly believe it will mitigate the need for them.

Chairman LAFALCE. If we are going to be using the GATT rules in our trade with Canada, which panel do we go to when that issue comes into dispute? Do we go to the GATT panel? Do we go to the NAFTA panel or the FTA panel?

Mr. ROH. Perhaps I could add a word on the legal relationship. The GATT has some rules on what you can do in countervailing duties and subsidies and so forth. We will put those rules into—or we will apply those rules in our implementing legislation, and what U.S. administrator agencies will apply and U.S. courts will apply is U.S. law, and if we believe Canada is violating those rules or if Canada believes we are violating the rules of the subsidies code of

the GATT or of WTO, then we would probably go to that body. What Chapter 19 panels look at is compliance.

Chairman LAFALCE. So the United States and Canada could go to the WTO?

Mr. ROH. Sure, just as they can go to GATT now and do.

Mr. SMITH. Like in the pork case.

Chairman LAFALCE. In how many instances since January of 1989 have the United States and Canada gone to a GATT panel as opposed to a binational panel?

Mr. SMITH. Well, there is one specific instance in the case with respect to pork that was discussed earlier, the contentious Chapter 19 case that went to an extraordinary challenge there was also a GATT challenge by Canada about the provision of the U.S. law, but the GATT challenge dealt with a different matter.

What the binational panels do is replace traditional review of the existing domestic law. What the GATT challenge that Canada made was with respect to whether the U.S. law was in conformity with the international obligations.

So, that continuation of that dual system with the binational panels for the application of the law and appeal to the GATT, WTO for whether the law—about whether Canada or the United States is in conformity with the international obligations will continue and Chapter 19 doesn't preclude us from changing our law.

The panels have to apply our law as it may be changed over time. The discipline on what you can do with your law is—we didn't include that in—essentially we didn't include it. There are provisions where if we change our law, either party changes its law, you can go to a panel process that can give you a sort of a declaratory judgment on that point and whether it is consistent with the spirit of GATT rules, but the right of that is to observe the golden rule, which is to unto—they can't stop us from changing our law.

They can imitate our sins and vice versa so there isn't any inconsistency. You can have a Canadian challenge saying our law is not in conformity with the GATT obligations, and a second challenge that is really being brought by the private practitioners saying we are misapplying that law that is going before the NAFTA panel or the CFTA panel.

Mr. ROH. That is the problem when you get a couple of litigious countries. They create too many ways to handle dispute.

Chairman LAFALCE. We are going to bring this to a close. I think it is good that periodically we get together to discuss the progress of this trade relationship because it is, as far as I am concerned, the most important trading relationship in the world, certainly the most important trading relationship for both our countries.

I think it behooves us to always remember that and treat each other with a tremendous amount of respect and deference. Sometimes we have to remind some of our own officials of that. Sometimes the Canadians might have to also.

Sometimes both our officials should work harder at remembering that 99.9 percent of our relationship is a very, very positive, very, very positive relationship, a very, very positive experience, and that it is inevitable in even the best relationship in the world that there will be disputes. So, long as we have an effective dispute resolution

mechanism, that is the best that a fallible world can hope for. Thank you very much.

[Whereupon, at 11:32 a.m., the committee was adjourned, subject to the call of the chair.]

APPENDIX

OPENING STATEMENT
Congressman John Conyers, Jr.

Small Business Committee
Hearing on United States-Canada Trade
June 9, 1994

Thank you Chairman LaFalce for holding this important hearing on United States-Canada trade under NAFTA and the US-Canada Free Trade Agreement. I am pleased that the scope of this hearing covers the FTA, because during the NAFTA debate, so much time was spent on US-Mexico trade that I think our neighbors to the north were neglected somewhat.

US-Canada trade is critical to my home state, Michigan. Michigan's exports to Canada, have increased 30 percent since the United States entered into the bilateral FTA. Even before the FTA, exports such as metals, transportation equipment, electronics, and non-electric machinery made Canada Michigan's biggest export market. Economic growth measured by export numbers has been good under the FTA. But I know from my years in Congress that the formula for progress is often more complicated.

There are some concerns with environment. The Canadian paper industry has challenged U.S. recycling laws as barriers to trade, and metal recycling laws could come under challenge. Another example is Article 904 of the US-Canada Free Trade Agreement which forbids both governments from placing any restrictions on energy exports except in rare cases involving "national security." This provision lead to the exploitation of waterways for hydroelectric power and natural gas for export to the U.S. We have an long standing strong relationship with Canada, and I know these trade disputes represent small chapters, but I am interested to hear more.

There is a delicate balance between progress and profit. I look foward to hearing from the witnesses how we can strike such a balance through the trade mechanisms we are discussing today.

STATEMENT OF REP. JOHN J. LaFALCE

COMMITTEE ON SMALL BUSINESS

"United States-Canada Trade Under the FTA and NAFTA"

June 9, 1994

The Small Business Committee convenes this morning to examine the status of United States-Canada trade relations, and how the two countries have fared under the provisions of the Free Trade Agreement (FTA) operative since January 1989 and now subsumed into the North American Free Trade Agreement.

I was a strong proponent of the FTA in 1988, and continue to believe it was an enormous step forward in liberalizing trade relations and promoting economic growth in both countries. I have seen my own region of Western New York benefit enormously from new opportunities for trade in both goods and services. This year, in fact, is the first time an American, Tom Daly--from my district--is president of the U.S.-Canada Business Association. And last month in Niagara Falls, the Can-Am Border Trade Alliance was launched to address a broad range of issues affecting the flow of trade and tourism across the border.

Canada is the United States' largest trading partner. According to the U.S. Department of Commerce and to Statistics Canada, two-way trade has grown at double-digit rates since FTA implementation, rising 14 percent in 1993 over the previous year to nearly $220 billion. U.S. manufacturers increased their penetration of the Canadian market to 29.6 percent in 1991-92, up from 26.4 percent in 1989-90. Canadians also increased their manufacturing share of the U.S. market by 0.1 percent.

The trade agreement has further expanded trade opportunities between our two countries in services and government procurement through greater liberalization measures. New provisions also strengthen intellectual property protection, and greater coverage of land transportation services broaden opportunities in this sector.

Even with the substantial increase in trade between our two countries, the lowering of barriers to goods, services, and people flowing across our borders, and the impressive new cooperative efforts of like-minded groups in both countries, this important effort to enhance bilateral trade relations has not been without its problems. The list of bilateral trade disputes is lengthy, and the dispute settlement mechanism has proved somewhat cumbersome. As part of today's hearing, we want to examine whether the dispute resolution process that was

negotiated and the U.S. Congress approved is operating as intended.

Questions have been raised as to how the panels have functioned and whether they have followed the mandate of reviewing whether respective laws have been applied correctly--not whether the laws themselves are correct. The Committee is interested in ways the panel system might be improved to make the process for traders on both sides of the border an easier, faster means for resolving disputes.

Two weeks ago, Canadian Trade Minister MacLaren and USTR Kantor discussed the possible development of alternative trade remedy proceedings. We would like to hear from our witnesses what "alternatives to trade remedy rules" are under consideration. Obviously, changes to these procedures and the recourse in resolving trade conflicts they provide will affect the business community and small business in particular.

This morning to provide us with expert perspectives on U.S-Canada trade, we have an excellent panel of witnesses. **Charles E. Roh** is the Assistant U.S. Trade Representative for North American Affairs, and as such is the key U.S. official directly responsible for our bilateral trade relationship. Mr. Roh was also directly involved in passage of the FTA implementing legislation in 1988.

Mr. Paul Joffe, Principal Deputy Assistant Secretary for Import Administration at the U.S. Department of Commerce, is responsible for overseeing U.S. trade laws and has close experience with dispute resolution panels.

Finally, **Professor Murray Smith,** Director of the Center for Trade Policy and Law at Carleton University in Ottawa, has extensive experience in U.S.-Canada trade relations.

We welcome all of you this morning.

Statement of Representative Jan Meyers
Hearing on U.S.-Canada Trade Relations
Committee on Small Business
June 9, 1994

Mr. Chairman, today the committee conducts another session on a most important topic - U.S.- Canada trade relations. The world market is now truly a reality. This situation will undoubtedly cause some dislocation in all industrialized nations. To be competitive nations must seek a pro-entrepreneurial outlook and reject anti-growth taxation, regulatory, and general government mandate policies. As our own country ventures forth in the new world atmosphere, we must do our utmost to secure fair and prosperous trade policies with our nearest neighbors first.

The U.S.-Canada Free Trade Agreement and the recent NAFTA agreement are two very positive steps in this direction. This morning we will focus on our relations with Canada. In reviewing today's testimony, I was particularly impressed with the statement of Murray G. Smith. Utilizing solid economic facts Mr. Smith paints a very positive picture that has developed for both nations as a result of our trade agreement. He then goes on to make a most salient point. Many Canadian economists view the agreement favorably, yet the Canadian public itself has a different perception. In fact, many Canadians blame their country's lingering recession on the free trade agreement. This presents policy makers such as ourselves a valuable lesson. It is a difficult task, at best, to produce positive economic policy. Part of this task should include the education of the public with the appropriate economic results of each and every policy.

STATEMENT OF CONGRESSMAN JIM RAMSTAD BEFORE THE HOUSE SMALL BUSINESS COMMITTEE U.S./CANADIAN TRADE RELATIONS UNDER THE CFTA AND NAFTA

June 9, 1994

Thank you Mr. Chairman for calling this hearing today. I also want to welcome our distinguished panelists.

I am certainly pleased to hear that our trading relationship with Canada has improved dramatically since the enactment of the U.S.-Canada Free Trade Agreement (CFTA), which took effect on January, 1989.

I was also pleased by Charles Roh's comment in written testimony that the NAFTA improved on the CFTA not only in adding the larger and growing Mexican market to the free trade area, but also in stronger substantive provisions that expand on our previous relationship with Canada.

I also appreciate our panelists' general expertise on trade matters and I am anxious to hear their thoughts on the Uruguay Round agreement.

Again, thank you for calling this hearing Mr. Chairman.

OPENING STATEMENT
THE HONORABLE BILL SARPALIUS

Good morning. Thank you Mr. Chairman for holding this hearing. As you know, as the former Chairman of the Small Business Subcommittee on Rural Enterprises, Exports and the Environment, I am extremely interested in this issue.

I learned a lot during the three hearings we held on small businesses and exports. One thing that I found most distressing was that less than 10 percent of all American small businesses are involved in exporting. Small businesses must export to stay competitive, to grow and to diversify.

The growth of small business means growth for America, i.e. more jobs. Further, export related jobs tend to be high-wage jobs. Since small businesses account for just over half of all the jobs in America, increasing small

business exports could result in the creation of many high-wage positions.

I appreciate the participation of the witnesses today. I am interested to hear what you believe NAFTA has done to help small businesses export to Canada and, secondly, whether or not you believe more jobs have been created due to the passage of NAFTA.

Again, thank you Mr. Chairman.

QUESTIONS

1) Has NAFTA changed the way small businesses look at exporting? Do they see the process as less frightening?

2) Has the Administration done anything to help encourage small businesses to export -- have you tried to make the process less bureaucratic?

Statement of Paul L. Joffe,
Deputy Assistant Secretary of Commerce for Import Administration,
before the Committee on Small Business
U.S. House of Representatives

Thursday, June 9, 1994

Good morning Mr. Chairman and members of the Committee. I am Paul L. Joffe, Deputy Assistant Secretary for Import Administration at the Department of Commerce. I appreciate this opportunity to speak on the matter of U.S.-Canada trade relations and certain procedures established first under the U.S.-Canada Free Trade Agreement (CFTA) and now under the North American Free Trade Agreement (NAFTA) that affect our administration of the unfair trade laws.

The trading relationship between the U.S. and Canada is of great importance to our economy. A cornerstone of this relationship has been the free trade agreement between our two countries. Both countries have been able to benefit from the free trade agreement through increased investment and jobs. Since implementation of the CFTA in 1989, we have experienced significant benefits.

- U.S. merchandise exports to Canada grew by $28.6 billion, from $71.6 billion in 1988 to $100.2 billion in 1993.
- Canadian direct investment in the U.S. rose $12.3 billion between 1988 and 1992.
- U.S. exports have shot up in sectors which faced high tariffs before the CFTA, and in 46 of 98 product categories exports grew 100 percent or more.

We fully expect these results to continue between now and 1998 when all tariffs between the U.S. and Canada will be eliminated. Overall it is safe to say that the CFTA has been a success and we can expect similar results from NAFTA.

This growth in trade has come about as a result of increasingly open markets. While trade frictions have not been eliminated, they have been reduced in certain respects. The number of antidumping orders issued has dropped from 12 during the period 1984-1988 to eight from 1989-1993. In addition, the number of orders revoked has increased, from zero during the period 1984-1988 to nine during the period 1989-1993. This is an expected result, as the conditions which allow dumping to occur are being mitigated. Considering that Canada is our largest trading partner, we have remarkably few antidumping cases involving Canadian exports.

With this overall picture in mind, let me address developments under the CFTA and NAFTA as they affect our responsibilities for administration of the antidumping and countervailing duty laws. In particular, I will discuss (1) the Chapter 19 binational review process, (2) the proceedings in the swine, pork, and lumber cases, (3) and prospects for the panel review process under the NAFTA.

Chapters 19 of both the CFTA and the NAFTA establish binational dispute resolution procedures in matters involving antidumping (AD) and countervailing duty (CVD) actions. In the country taking the antidumping or countervailing duty action,

parties have recourse under Chapter 19 to binational panel review as an alternative to judicial review.

Binational panels review the same body of facts and evidence and employ the same standard of review as do the courts of the importing country. A panel either affirms the challenged AD/CVD determination or remands it for action not inconsistent with the panel's decision. Panels follow a common set of well-defined rules and procedures and have approximately one year to render a final decision, which is binding on the parties to the dispute.

To protect the integrity of the binational panel review system, panel decisions under certain circumstances may be subject to review by an extraordinary challenge committee (ECC). Upon request by an affected CFTA or NAFTA signatory, an ECC can review a panel decision for gross misconduct by a panelist, a serious departure by the panel from a fundamental rule or procedure, or for whether a panel has manifestly exceeded its powers, authority or jurisdiction. If an ECC finds that any of these actions has materially affected the panel's decision and threatens the integrity of the binational panel review process, the ECC may vacate the original decision or remand it to the original panel for action not inconsistent with the ECC decision. If the ECC vacates the original decision, a new panel is convened.

These are the basic elements of the binational panel review process that are common to both the CFTA and the NAFTA. The NAFTA, in addition, includes several improvements over the CFTA. The NAFTA encourages the selection of retired or sitting judges (over trade lawyers, economists, and policy experts with no judicial review experience) to serve on panels. Judges, the countries felt, may better recognize the need for and importance of respecting Congressional intent and an agency's expertise when reviewing an administering authority's decision. The NAFTA also strengthens ECC review by (1) giving extraordinary challenge committees more time to render a decision and (2) clarifying that the grounds for bringing an extraordinary challenge include failure to apply the appropriate standard of review.

Finally, the NAFTA includes a new process for safeguarding the panel review system. Specifically, Article 1905 permits review, by three-member special committees, of allegations of one country that another country has interfered in the proper functioning of the panel system, for example by preventing the establishment of a panel or not enforcing a panel decision. If a special committee makes an affirmative finding, the countries will either negotiate a solution or the complaining country may suspend the operation of Chapter 19, subject to retaliatory suspension by the offending country.

The binational panel review system will be especially important for U.S. exporters who become involved in antidumping and countervailing duty cases in

Mexico. Because of the binational panel system, Mexico has had to make many substantive changes in its laws and in its system for judicial review in order to grant to U.S. exporters due process protections equivalent to those that Mexican exporters have in U.S. courts. The binational panel system, therefore, has already resulted in major benefits to our businesses trading with Mexico.

The panel process has other beneficial potential. For example, the panel process is generally more expeditious at settling disputes than national court systems. The panel process has been favored by exporters of both Canada and the United States. While the free trade agreement continues to allow a party to bring a case under the national court systems, the majority of parties have chosen to pursue the panel process.

Turning from the binational review process to discussion of some specific panel decisions, I will briefly discuss the swine, pork and lumber cases.

The Chapter 19 binational panel review process of the CFTA went into effect in January of 1989. Since that time, there have been 19 panel decisions issued in the United States and Canada in cases involving antidumping and countervailing duty determinations. Of these 19 decisions, three have been challenged by the United States before Extraordinary Challenge Committees. These three challenges involve Fresh, Chilled or Frozen Pork, Live Swine, and Lumber. The Pork case involved a

challenge to the International Trade Commission's threat of injury determination, while the Swine and Lumber cases involved primarily the issue of specificity. That is, they involved whether a subsidy has been provided to a specific enterprise, industry or group of enterprises or industries, which is a pre-condition to finding a subsidy countervailable.

The ECCs in both the Pork and Swine proceedings dismissed the challenges for failure to meet the standards for extraordinary challenge under the Free Trade Agreement. The committee in the Swine extraordinary challenge, however, did admonish panels to adhere strictly to their proper roles, apply the appropriate standard of review, and not create changes in the law. The Lumber case is ongoing, and oral argument is scheduled to take place next week. Notably, all three cases involve agricultural or natural resource products. Furthermore, the Swine and Lumber disputes both involve the issue of specificity.

The panels in the Pork, Swine and Lumber cases did not function in significant respects as the U.S. government would have hoped. In other respects, the binational panel mechanism generally is functioning as intended under the Agreement. Panels reviewing final antidumping and countervailing duty determinations in place of domestic courts have expedited the review process, issuing decisions within set deadlines. American producers and exporters have taken advantage of the expedited process, participating in both U.S. and Canadian panel proceedings.

The experience of the Department of Commerce with panels generally has been that we do not win or lose more issues than we do in the domestic courts. Of the 15 panel decisions regarding United States agency determinations, four affirmed the agency's determination without remand. In the January 24, 1990 decision in Replacement Parts for Paving Equipment, for example, the panel properly discussed the standard of review, the evidence on the record, and the history of the order and determined that Commerce's scope determinations were reasonable and supported by the record. In Pure and Alloy Magnesium, which the panel affirmed in part and remanded in part, and then unanimously affirmed on remand, the panel first discussed the appropriate standard of review and each issue appealed to the panel. The panel then properly followed the binding precedent of a decision of the Court of Appeals for the Federal Circuit. On an issue involving specificity, this panel discussed deference to an agency interpretation, the court cases on the issue, and the Lumber panel decision on the issue. In the opinion of the Department, this panel then properly gave deference to the agency interpretation of specificity and, while discussing the Lumber panel decision, properly stated that it was not binding precedent and appropriately did not follow it.

Panel decisions are not precedent for other panels or for courts and it has been our experience that panels do not rely on other panel decisions as binding precedent. For example, even though the panel in Swine rejected the U.S. government interpretation of the specificity test, the panel in Magnesium unanimously affirmed the

U.S. government interpretation of that same test. The panel rulings have not resulted in a change in the U.S. interpretation of the law on this issue or in its application in any other cases.

Given this record, we would not conclude that because we have had three extraordinary challenge cases that the system, on the whole, is not working. As noted earlier, the panel process does have potential benefits. Of course, the process can be improved, and we are committed to doing that as part of our implementation of the larger free trade agreement which is greatly benefitting the United States, as well as Canada and Mexico.

The Administration is committed to a strategy of trade liberalization to boost U.S. economic growth. NAFTA and the Uruguay Round Agreement are important elements of this strategy, along with bilateral efforts to open markets in Japan, China, and elsewhere. Through freer trade and more open markets worldwide we can achieve greater U.S. exports and increased American jobs. At the same time, we will maintain the strength and effectiveness of our antidumping and countervailing duty laws. Liberalization of trade can only be sustained if it is not accompanied by unfair practices that undermine employment and competitiveness. As we work for the benefits of expanding trade, we remain dedicated to maintaining strong unfair trade laws and vigorous enforcement of American rights under domestic law and international agreements.

S U M M A R Y OF

TESTIMONY OF CHARLES E. ROH, JR.
ASSISTANT U.S. TRADE REPRESENTATIVE FOR NORTH AMERICAN AFFAIRS

BEFORE THE COMMITTEE ON SMALL BUSINESS
U.S. HOUSE OF REPRESENTATIVES

June 9, 1994

Mr. Chairman, I welcome the opportunity to appear before the Committee on Small Business today to discuss the U.S. - Canada trade relationship and the operation of the U.S. - Canada Free Trade Agreement and its broader successor, the North American Free Trade Agreement (NAFTA).

The U.S. - Canada Trade Relationship

Canada has long been our largest trading partner, by a large margin. That trade relationship has grown since we agreed to create a free trade area. The U.S. - Canada Free Trade Agreement (CFTA), which took effect on January 1, 1989, created the world's largest and most comprehensive bilateral free trade area. Building on the success of that agreement, the United States, Canada, and Mexico created the North American Free Trade Agreement, which entered into force on January 1, 1994, superseding the CFTA. The NAFTA improved on the CFTA not only in adding the large and growing Mexican market to the free trade area, but also in stronger substantive provisions that expand on our previous relationship with Canada.

Let me give you just a few of the statistics that show the size and dynamism of the U.S.-Canadian economic relationship:

-- Total merchandise trade with Canada exceeded $211 billion dollars in 1993; with our next largest trading partner, Japan, merchandise trade was less than $156 billion dollars in 1993.

-- While The United States has run deficits in its merchandise trade with Canada, $9.7 billion in 1992, we enjoyed a healthy surplus in services exports, $9.1 billion in 1992.

-- Exports to Canada were estimated to support some 1.5 American jobs in 1992.

-- Goods exports to Canada rose nearly 40 percent from 1988 to 1993, from $71.6 billion to $100.2 billion. This increase in trade is all the more remarkable in light of the low rate of growth in overall GNP,

especially in Canada, in the early 1990's.

The CFTA and NAFTA

As you know, when the NAFTA entered into force on the first of January of this year, the CFTA was suspended. The NAFTA builds on the successful U.S.-Canada FTA, generating new opportunities for economic growth for all three countries of this continent. NAFTA creates a free trade area of over 370 million people with a total output of over $7.2 trillion in goods and services.

The United States and Canada decided to suspend the CFTA upon entry into force of the NAFTA because the NAFTA incorporates directly, or in improved form, all the provisions that had existed in the CFTA. For example, the NAFTA incorporates completely the CFTA's tariff phase-out schedules for U.S.-Canada trade, under which we have already largely eliminated duties on goods traded between our two countries. Duties that remain, those that were on a ten year phase-out schedule, will be eliminated on January 1, 1998. For many of the rules on non-tariff barriers, NAFTA modifies CFTA rules only slightly, to account for their application to Mexico, or to improve wording. For example, NAFTA largely incorporates the CFTA's provisions governing bilateral trade in alcoholic beverages, agricultural products, automotive products, non-tariff barriers, temporary entry of professionals and energy. The wording The CFTA provisions regarding the "cultural industry" exception, including the right of the United States to take off-setting action of commensurate value in response to Canadian actions to protect cultural industries remain unchanged.

Dispute Settlement

In any relationship as large as that of the United States and Canada, disputes are probably inevitable, even with strong free trade rules. We should not underestimate the importance of the issues to the constituencies affected on both sides of the border, but both governments also need to make efforts to assure that we settle our differences in a way that is fair and that does not harm the overwhelmingly successful and mutually beneficial relationship.

It is worth noting that many of the most serious disputes have occurred in areas not fully addressed by the CFTA or absent from it all together. It is worth recognizing that these disputes tend to occur in areas where less liberalization was accomplished or exceptions were made in the free trade rules. For example, there have been frequent frictions on products such as beer, softwood lumber, and agriculture -- all areas of relatively high government intervention where the FTA negotiators were unable to come to full agreement.

The NAFTA's dispute settlement mechanisms do provide a means to

help resolve frictions.

The NAFTA incorporates with some improvements the CFTA mechanism in Chapter 19 for independent binational panels to review final U.S. and Canadian (and Mexican) AD and CVD determinations. By the end of 1993, 48 panels had been convened pursuant to the provisions of CFTA Chapter 19, 28 of which have been completed. Twenty cases are currently active. These involve imports of steel, softwood lumber, and magnesium from Canada, and exports of gypsum board, steel, pipe, and carpeting from the United States. It should be noted that Chapter 19 panels are initiated by the private sector rather than governments, and the private sector on either or both sides of the issue will quite properly invoke this mechanism any time they would otherwise have gone to court. This produces a large number of cases, which are sometimes erroneously equated with inter-governmental disputes, and which in turn leads some to think we have more disputes with Canada than with other countries.

By contrast, there have been remarkably few disputes between the United States and Canada under the normal intergovernmental dispute settlement mechanisms of CFTA Chapter 18 or its successor Chapter 20 of the NAFTA. These mechanisms deal with disputes regarding the interpretation and application of the NAFTA rules. If a dispute cannot be resolved by consultations, a panel of private sector experts will be convened. As in the case of the GATT, a party cannot be compelled to comply with a panel recommendation, but the aggrieved party will have the right to retaliate if there is no agreed redress. There were five Chapter 18 cases completed under the CFTA. No dispute has as yet gone to a panel under NAFTA rules.

NAFTA BROADENS SCOPE OF CFTA TO NEW AREAS

NAFTA broadens the scope of the CFTA to new areas:

-- The **intellectual property chapter** of NAFTA provides world class standards of protection for patents (20 years), trademarks, copyrights, sound recordings, satellite signals, industrial designs, semiconductor integrated circuit designs, and trade secrets.

-- The **land transportation chapter** covers truck, bus, rail, intermodal terminals, warehousing, and landside port services.

-- The **supplemental agreements on labor and the environment** are ground-breaking. The fundamental objectives of the labor and environment agreements are to work cooperatively to improve national enforcement of national laws relating to labor and the environment. They commit all three nations to fair, open and equitable administrative and judicial processes for the enforcement of environmental and labor laws.

NAFTA also enhances the CFTA. Some of the most notable improvements of NAFTA over the CFTA include:

-- The **rules of origin chapter** clarifies and simplifies many rules and record keeping requirements; raises the minimum value added content requirements, where applicable (from 50% to 62.5% for automobiles), to ensure high levels of North American content.

-- **Government procurement** principles, procedures, and threshold for goods remain unchanged, but coverage has been expanded from the CFTA to include more entities and most services, construction services, and Federal Crown Corporations (such as the Royal Canadian Mint and Canadian National Railway).

-- **Dispute settlement** procedures under the CFTA are expanded and strengthened to further ensure fair, equitable, and timely resolution of disputes, especially those involving interpretation of NAFTA and application of trade remedy laws.

NAFTA IMPLEMENTATION

Implementation of the NAFTA is off to a good start, especially considering the changes necessary and the short time available to put it into place. The challenge for Mexico has probably been greatest, because the United States and Canada had the experience of the CFTA already behind us. While there have been occasional problems, all three countries have been working hard to address them quickly. We remain committed to working with our private sector and the Governments of Canada and Mexico to make the agreement work effectively.

While it is much too early to judge the full impact of the NAFTA, it is heartening to see that trade statistics for January through March do show trade growing throughout the continent. U.S. exports of goods to Canada increased by 9 percent over the same period last year, and imports of goods from Canada grew 8.5 percent. The growth in our trade with Mexico was even more marked in this period, despite slow growth in Mexico's economy.

We have initiated an expedited negotiation to further accelerate the tariff reductions for some NAFTA products. This should provide real benefits for exporters in all three countries. In three rounds of similar negotiations under the U.S. - Canada FTA, the U.S. and Canada agreed to eliminate duties affecting approximately $9 billion worth of two-way trade ahead of schedule, with the full support of industry and labor on both sides of the border.

NAFTA Supplemental Agreements on Labor and the Environment

The Commissions on Labor and Environment established in the NAFTA Supplemental Agreements are also off to a good start. The three governments' National Administrative Offices (NAOs) have been open for business since January 3 within their labor departments. Labor Secretary Bob Reich met with his counterparts on March 21 in Washington, and announced that Dallas will be the site for the Labor Secretariat. The Labor Ministers have also made significant progress in defining the organizational structure and functions of that Secretariat. EPA Administrator Carol Browner joined the Canadian and Mexican environmental ministers in Vancouver, B.C. for their inaugural meeting on March 23, where they made good progress on institutional issues. Montreal will be the site for the Environmental Secretariat. On April 15 the Department of Labor announced it would investigate two submissions regarding alleged violations of Mexican Labor law, one from the Teamsters and the second from the United Electrical Workers, that it received in February. Both concern Mexican subsidiaries of U.S. firms. DOL has up to 180 days in which to conduct its investigation.

BENEFITS FOR SMALL BUSINESS

For small business, the easiest way to get into profitable international trade may well be with our geographic neighbors. NAFTA will help small business by reducing barriers to trade and investment, making their goods and services more competitive. Let me give you just a few specific examples:

-- Tariff reductions are an obvious benefit to small businesses. Those who are exporting are all seeing the costs of their products to their customers reduced, thereby making them more competitive. Importers will be able to source them at lower costs as well.

-- Strong protection of intellectual property rights under NAFTA is another benefit. Intellectual property was largely left out of the CFTA while NAFTA has strong rules. Among others, software producers, copyrights and patents will be protected, and NAFTA requires enforcement mechanisms.

-- NAFTA rules of origin will be easier for companies to use than the U.S.-Canada Free Trade Agreement rules of origin. To the extent possible, rules are based on tariff shifts. There are now fewer rules requiring cost accounting, and those that do require such calculations are based on simpler formulas.

In conclusion, let me re-emphasize the tremendous importance we attach to the U.S.- Canadian trading relationship. Though the occasional frictions get most of the media attention, this relationship has further strengthened under the CFTA. NAFTA builds on the success of the CFTA and will benefit all three countries.

Testimony Before the Small Business Committee
of the United States House of Representatives

Canada-U.S. Trade Relations with Free Trade

by

Murray G. Smith*

June 9, 1994

* Director, Centre for Trade Policy and Law, Carleton University and the University of Ottawa, Ottawa.

Canada-U.S economic relations aren't broken, but there are some strong pressures on the relationship and serious outstanding problems which if they are not resolved could have serious and damaging repercussions. Some of the sources of pressures are perceptions, while others stem from difficult policy issues that both countries need to address.

The Good News

If we look at the numbers, one must be struck by the overall balance in the trade and economic relationship between Canada and the United States. In 1993, the U.S. Department of Commerce indicates that the United States had a surplus on current account of $1.0 billion on total bilateral flows of goods, services and investment income in excess of $250 billion. This overall bilateral balance is the more remarkable because both countries have substantial current account deficits with the rest of the world.

Of course, there are different bilateral balances within the current account. The United States had a bilateral surplus of $7.7 billion on services and $6.2 billion on investment income, while Canada had a bilateral surplus of $12.5 billion on merchandise. In turn within the Merchandise trade account, Canada had a surplus on energy and industrial materials trade while the United States had a surplus on capital goods.

Looking at trade flows, as an economist I conclude that the FTA has worked well to the mutual benefit of both countries in stimulating trade and economic growth amidst the prolonged recession of the early 1990s. For example, U.S. exports of capital goods to Canada surged 50 percent from 1988 before the FTA to $30 billion in 1993, while similar U.S. exports to Europe expanded only 20 per cent over the same period. At the same time, Canadian exports of capital goods to the United States surged $6 billion to

$14 billion. Many enterprises, both large and small in both countries have responded to the competitive challenges and opportunities resulting from the removal of trade barriers between Canada and the United States.

So where are the problems?

Unfortunately, however, public perceptions in Canada have not reflected a careful analysis of trade patterns. To many Canadians the FTA is associated with, and for many perceived as a major cause of, the lingering recession of the 1990s. Furthermore every trade dispute, whatever its ultimate outcome, has served to remind Canadians that the FTA did not, and the NAFTA will not, solve all problems. To many Canadians, the persistence of high-profile trade disputes confirms concerns that NAFTA (like the FTA before it) provides lopsided benefits to the United States. Canadian opposition to NAFTA reflected continued concerns about the perceived vulnerability of Canada to the United States much more than concerns about potential Mexican competition.

In contrast to the Canadian public who seem to perceive every trade dispute as Canadians being harassed by litigious Americans, most Canadian specialists (and many American specialists also) have a favourable assessment of the dispute settlement mechanisms under the FTA, which are continued under NAFTA. In particular, among the specialist communities of the trade bar and academics in both countries, the Chapter 19 process has acquired credibility for providing fast and effective review of the administrative agencies according to the appropriate standard of judicial review in the domestic law of each country. However the acrimony over the softwood lumber dispute threatens to damage the process.

Unfortunately, an overall trade balance within a sector is not sufficient to assure harmonious trade relations. The Commerce Department indicates that the United States exported $5.9 billion to Canada and imported $5.6 billion in food, feeds and beverages in 1993, yet the agrifood sector is a source of serious frictions between Canada and the United States.

Bilateral agricultural issues have proved very difficult to resolve and the recent tour of Latin America by the U.S. Secretary of Agriculture seeking to recruit countries to launch antidumping and countervailing duty cases against Canadian exports of wheat was seen as counterproductive in Canada.

How did we get here? In the Canada-U.S. Free Trade Agreement the two countries agreed to remove tariffs and some non-tariff barriers on bilateral agricultural trade as well as removing export subsidies from bilateral shipments. However, the tough issues, quota restrictions on sugar, dairy, and peanuts in the United States and on dairy and poultry in Canada; domestic farm subsidies; or agricultural export subsidies in third markets were put aside to be dealt with in the Uruguay Round.

Unfortunately the Uruguay Round was delayed and implementation will not start until 1995. In the meantime, bilateral frictions have festered. Export subsidies such as the U.S. Export Enhancement Program and Canada's Western Grain Transportation Assistance will be reduced, but not eliminated by 2002. Reflecting concerns of dairy farmers who are concentrated in Quebec and poultry farmers, Canada is converting import quotas into high tariffs under the Agriculture chapter of the World Trade Organization(WTO). The United States is imposing tough restrictions on sugar-containing and peanut products from Canada and is seeking significant tariffs on wheat from Canada.

Some U.S. farm groups perceive that Canada obtains lopsided benefits from the Canada-US FTA agricultural chapter, which is continued under NAFTA. Although the overall levels of subsidies in the key commodity groups may be similar in the two countries, and in some cases Canadian subsidies are much lower, differences in the farm programs, administrative arrangements, and delivery mechanisms are sources of perceptions of unfairness. The Uruguay Round rules for agricultural subsidies are an important step, but only a step, toward resolution of these problems.

In addition to continuing problems over agricultural subsidies, the commitment to develop a new regime for subsidy and countervailing duty measures as well as antidumping rules, which was mandated in the Canada-U.S. Free Trade Agreement, was not included in the same form in NAFTA. However, the new Canadian government indicated that completing the unfinished business under the FTA is a high priority and thus sought and received strong assurances from the U.S. Administration that a working group would deal with these issues over two years, before Canada proceeded with the implementation of NAFTA on January 1.

In my view the Uruguay Round and the WTO provide a very useful basis for dealing with subsidies and countervailing duties in a North American context. Certainly the WTO chapter on subsidies and countervailing duties offers a useful basis for introducing limits on the use of subsidies which is necessary if there are to be changes in countervailing duty laws. Since Canada and Mexico tend to be suspicious of potential or perceived U.S. political dominance, it is useful to have a framework of multilateral rules and a multilateral oversight mechanism about which types and levels of subsidies are permitted, which can provide a basis for a trilateral arrangements.

The Antidumping chapter of the WTO, if implemented faithfully, will have modest impact upon the application of antidumping laws within NAFTA. However, there is great concern in Canada among the private sector and within governments that the Uruguay Round implementing legislation in the United States laws will seek to exploit any ambiguity in the international arrangements in order to create a more protectionist regime for antidumping and

countervailing duty laws.

The Canadian government is committed to making progress on the unfinished business under the FTA and NAFTA as is evident from recent speeches by the Trade Minister Roy MacLaren. The most obvious focus for further work is on the application of the antidumping laws, because it may be difficult to go much further with respect to subsidies and countervailing duties than is achieved in the WTO, and because the removal of tariff and non-tariff barriers within NAFTA changes the rationale for antidumping laws. Although the Chapter 19 process seems to have worked relatively well, judicial review under the existing laws is not a substitute for better and more clearly defined trade rules.

Good faith implementation of the Uruguay Round is a necessary, but not a sufficient condition for maintaining mutually beneficial and harmonious trade and economic relations. Canada and the United States will need demonstrate good will to avoid any fallout from the softwood lumber dispute, will need to work harder to resolve outstanding bilateral agricultural trade and subsidy issues, and make greater effort to find common approaches to the application of trade laws, especially antidumping laws within NAFTA. Policymakers need to keep in perspective the overall balance in this enormous and vibrant bilateral economic relationship and keep in mind the mutual benefits to be derived from building upon the present level of cooperation.

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